U.S. Bankruptcy Court
Eastern District of Michigan (Detroit)
Bankruptcy Petition #: 13–53846–swr

Date filed: 07/18/2013

Assigned to: Judge Steven W. Rhodes
Chapter 9
Voluntary
No asset

Debtor In Possession
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WAYNE–MI
Tax ID / EIN: 38–6004606

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Filing Date	#		Docket Text
12/26/2013		2313	Transcript Order Form of Hearing October 15, 2013, Filed by Creditors Detroit Fire Fighters Association, I.A.F.F. Local 344, Detroit Police Command Officers Association, Detroit Police Officers Association. (Eisenberg, David) (Entered: 12/26/2013)

UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF MICHIGAN

TRANSCRIPT ORDER FORM

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Case/Debtor Name:

Case Number: 13-53846

Chapter: 9

Hearing Judge Hon. Steven Rhodes

(•) **Bankruptcy** ( ) **Adversary**

( ) **Appeal** **Appeal No:** _____

Hearing Information (A separate form must be completed for **each** hearing date requested.)

Date of Hearing: 10/15/2013 **Time of Hearing:** 9:00 a.m. **Title of Hearing:** Eligibility Hearing

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UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF MICHIGAN
SOUTHERN DIVISION

IN RE: CITY OF DETROIT, MICHIGAN,	.	Docket No. 13-53846
	.	Detroit, Michigan
	.	October 15, 2013
Debtor.	.	10:00 a.m.
. . . . .		

HEARING RE. OBJECTIONS TO ELIGIBILITY TO CHAPTER 9 PETITION
BEFORE THE HONORABLE STEVEN W. RHODES
UNITED STATES BANKRUPTCY COURT JUDGE

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THE CLERK: All rise. Court is in session. Please be seated. Case Number 13-53846, City of Detroit, Michigan.

THE COURT: Good morning, everybody. I'd like to take appearances from the attorneys who will be speaking here today first. Can we do that?

MR. BENNETT: Thank you, your Honor. Bruce Bennett, Jones Day, on behalf of the city.

MS. NELSON: Good morning, your Honor. Assistant Attorney General Margaret A. Nelson on behalf of the State of Michigan.

MS. LEVINE: Good morning, your Honor. Sharon Levine, Lowenstein Sandler, for AFSCME.

MR. GORDON: Good morning, your Honor. Robert Gordon of Clark Hill on behalf of the Detroit Retirement Systems.

MR. MONTGOMERY: Good morning, your Honor. Claude Montgomery, Dentons U.S., for the Official Committee of Retirees.

MS. CECCOTTI: Good morning, your Honor. Babette Ceccotti, Cohen, Weiss & Simon, LLP, for the UAW.

MR. WERTHEIMER: Good morning, your Honor. William Wertheimer on behalf of the Flowers plaintiffs.

MS. PATEK: Good morning, your Honor. Barbara Patek of Erman, Teicher, Miller, Zucker & Friedman on behalf of the Detroit Public Safety Unions.

MS. CRITTENDON: Good morning, your Honor. Krystal Crittendon, interested party.

MS. BRIMER: Good morning, your Honor. Lynn M. Brimer appearing on behalf of the Retired Detroit Police Members Association.

MR. MORRIS: Good morning, your Honor. Thomas Morris of Silverman & Morris on behalf of the Retiree Association parties.

MR. GOLDBERG: Good morning, your Honor. Jerome Goldberg on behalf of interested party David Sole.

MR. TROY: Good morning, your Honor. Matthew Troy, Department of Justice, Civil Division, on behalf of the United States. It is not my intention to speak this morning, your Honor, unless you have specific questions regarding our filing from Friday.

THE COURT: Thank you, sir. Mr. Gordon.

MR. GORDON: Thank you, your Honor. I just wanted to provide the introduction relative to our proposed allocation of the time and order of presentation here this morning. As your Honor can see from the document that was filed, there are 11 objectors who wish to speak, and, of course, they all have important points to make, but -- and we very much appreciate the cooperation amongst all of them. It was a good and constructive process. Not only was that easy, but everyone has been very cooperative, and we've allocated

the time accordingly to various parties to have the opportunity to speak today.

You will note, your Honor, a couple things. One, we did not allocate the full 120 minutes in the morning. There's a few minutes left over. Similarly, in the afternoon there's about five minutes left over of the 90 minutes. That, of course, is not intended to necessarily waive our opportunity to have the full time, but we thought that would build in some flexibility and some error margin as people stand up and sit down to make sure that we fit within the time frame.

Also, as footnote one indicates, the presentation order does not necessarily tie -- correspond discretely with each of the issues as listed in your scheduling order, your Honor. There is some correlation, but various parties, as the Court, I'm sure, can understand, have a number of issues that they would like to address. There will be some overlap. The parties are going to try to overlap as little as possible, but it was not really feasible to try to identify discrete issues that each party was going to take on, so instead the hope is that as each party comes to the podium, they'll try to give you a little bit of a road map as to the particular issues that they're going to touch upon.

THE COURT: Thank you, and thank you for your extraordinary effort in coordinating this. I'm sure it was a

challenge. And I also want to thank all of the attorneys for cooperating with Mr. Gordon and with the Court in trying to organize this as best we can. So we're going to start then with AFSCME's counsel, and we're going to try to run the timing mechanism for your convenience. Kelli, have we got that available? I'm sorry.

MS. LEVINE: They were teasing me that if I'm nervous, it'll take 20 minutes, but if I remember to speak slowly, it'll take 35.

THE COURT: Okay. So for 35 minutes you may proceed.

MS. LEVINE: Thank you, your Honor. First, we appreciate the opportunity. We think these issues are extremely important, and we're glad that we have the opportunity to speak. Second, as Mr. Gordon correctly noted, the parties who are speaking here today have made a concerted effort to divide up the time and to try not to duplicate our comments, so in that regard we're reserving the right to rely on the filed objections along with the other arguments of other counsel simply because we won't have time to do it all ourselves.

With that, your Honor, we started this endeavor by looking at PA 436 specifically concerned, as you might imagine, with the pension issues and with the fact that we believe that the Michigan Constitution provides for

protections for vested pension benefits, and then that potentially conflicted with PA 436, and, therefore, we started looking at the issue of whether PA 436 was, in fact -- was, in fact, unconstitutional in that it allowed a Chapter 9 filing in light of the pensions -- in light of the pension restriction in the Constitution.

In addition to that, we were looking at the governor's authorization in allowing the Chapter 9 filing in light of PA 436 and in light of the Michigan Constitution and grappling with the issue of whether or not that authorization without any contingencies caused this Chapter 9 filing to be unconstitutional as applied.

In addition to that, we grappled with the ripeness issue as to whether or not all of these issues should be raised now or whether they should be raised in connection with a plan of adjustment, specifically, your Honor, grappling with the issue as it was presented to us by our members where we have folks literally sitting at their kitchen table deciding whether or not they can take medicine today or do they have to start taking it every other day, do they feed themselves, do they feed their children, do they pay rent, so we came to this Court anxious to have some of these issues decided quickly.

On top of that, as it turns out, involved in the mediations and the other efforts with regard to the serious

issues that are confronting Detroit, we do think understanding your Honor's views of the rules of the game could be useful for the parties in that process, but that's really by way of introduction because what we've done, your Honor, in addition to that, is we started researching how we thought PA 436 fit in the overall scheme of Chapter 9 and, in looking at those issues, delving into whether or not Chapter 9 itself was, in fact, unconstitutional, which is what we will address before your Honor this morning. And I'd like to, with the Court's permission, set the table a little bit but promise to get into Bekins and some of the cases that are cited by folks who disagree with our views later on in the comments.

So I'd ask you, your Honor, to come back with me, if you will, to elementary and high school when we first started talking about what the Constitution is and what it means, and, respectfully, when we go back, we remember that the framers of the Constitution were fleeing an oppressive, overbearing, centralized government. So when we started looking at how we framed our Constitution, we were very careful to make sure that there was a federal Constitution that was extremely limited only to specific rights that we believed should transcend every single state in the union, and we've come to call those the unalienable rights, and they refer to things like freedom of speech and freedom of

religion. And under the Tenth Amendment, your Honor, everything else is reserved for the states, so specifically reserved for the states are the state municipal governments' rights to handle their own financial management. And this is done, your Honor, not to protect the states, which would have been as suggested by the New Jersey plan, but was actually done to protect the individual citizens, as suggested by the Virginia plan, and the specific rationale behind protecting the individual citizens was in order to have accountability from our government and particularly, more importantly, from our local governments, which were viewed as being more accessible to the citizens that they were -- that they were supposed to be taking care of. So, for example, if somebody infringes on my right of free speech or my right of freedom of religion, I know I point my finger to D.C., and I look at the federal government, and I say to the federal government, who is accountable for those federally protected rights, "Make them stop," but if somebody says to me that there's an inappropriate use of the power over the financial management of a state municipality, of, for example, Detroit, I look to my local government. I look to my local politicians and my local leaders, and I say, "I'm holding you accountable," and we saw that working well very recently with the mayor of Detroit -- with the prior -- apologies -- prior mayor of Detroit, so this direct accountability, which is a

cornerstone of how we -- of how we run our country and how we run this democracy, is there for a reason, and it's not there to protect the states. It's there to protect the citizens. The Constitution doesn't start "We the states." It doesn't say, "I the general federal government." It starts, "We the People." So now, as we indicated in our brief, we believe there is what we've called this unholy alliance between the state giving authorization to the federal government to run this Chapter 9 process. And what we said there, your Honor, is that the states are, in essence, ceding the responsibility and the accountability for their own financial management, so by turning over under Chapter 9 to the federal government and being able to hide behind the bankruptcy process and this Court, we lose that accountability that's a cornerstone of what our Constitution requires of us, and we've seen that already. We saw that debtor's counsel correctly noted in an internal e-mail exchange back in January of 2013 that making this a federal issue provides political cover, and we've seen it in the depositions where we're talking to the EM and the governor, and they are talking about the fact that they're not exactly sure what's going to happen with the pensions. The bankruptcy process takes care of that. And we would respectfully submit, your Honor, that we're seeing play out in real time and real life the exact loss of accountability that the Constitution was designed to protect, so --

THE COURT: Well, but hasn't state consent been a cornerstone of the Supreme Court's Tenth Amendment jurisprudence?

MS. LEVINE: Your Honor, we'll talk about the consent in Bekins, and we don't believe that what we're saying here today is inconsistent with state consent. And if your Honor will give me a little bit more leeway, we'll reach that point --

THE COURT: Sure.

MS. LEVINE: -- because we understand the issue. So one of the comments that's being made is that in order for there to be -- that the reason why we can't do it at the state level, the reason why the state municipal governments can't do it is because it violates the contract clause, and by violating the contract clause, you can't do a plan of adjustment unless you have a hundred percent consent.

Now, we would respectfully submit, your Honor, that there's two responses to that, and they are -- and I'll admit they're diametrically opposed, but under either response you don't get to the place where you get to take it away from the states. Number one, if you believe, as suggested, that you need a hundred percent consent at the state level because of the contract clause, then we would respectfully submit that the states can't cede control to the federal government and then suddenly it becomes legal to do a plan of adjustment

without a hundred percent consent. And, your Honor, in doing that, we're actually just reading from the Constitution itself. The contract clause is in Section 10 of Article I of the Constitution. Section 10, Article I, of the Constitution has three subsections, one, two, and three. In the first section, it talks about no state shall enter into treaties with foreign countries, print money, and it's the contract clause. Under sections two and three, not where the contract clause sits, it says, "No State shall without the consent of Congress," so by the plain reading of the Constitution, if "no state shall" means no state shall, then no state shall do it with or without the consent of Congress, and the framers clearly understood that if they wanted the states to be able to do it with the consent of Congress, they could have done what they did in the two other subsections and basically said, okay, instead we'll do it -- we'll do it with a federal municipal bankruptcy statute where the federal government will consent, and, therefore, you can violate the contract clause. So our first point is under the contract clause, "no state shall" means no state shall, and if we're going to be intellectually honest with ourselves, that applies regardless of whether or not Congress consents because it's not, as in Section 10, the second and the third paragraph, "No State shall without the consent of Congress."

THE COURT: What Supreme Court case law supports

this interpretation?

MS. LEVINE: Your Honor, we respectfully submit that it's Ashton.

THE COURT: The case that Bekins overruled?

MS. LEVINE: Well, we don't believe that Bekins overruled it, and if I can keep going, the alternative approach -- and, frankly, the plain meaning of the statute we don't believe yet -- or I'll admit we haven't found yet a constitutional case that comes right out and says it is or it isn't done this way, but it is the plain reading of the Constitution, which we thought was --

THE COURT: Okay.

MS. LEVINE: -- a good place to start. But moving past that, let's assume -- and we believe the better answer is that there has to be a way to adjust debts. Then we go back to where we started, your Honor, which is this is absolutely a state municipal right. What Bekins was looking at -- and remember Bekins was decided in -- right in the middle of the Great Depression. Okay. And so up until the -- up until just before Bekins was decided, there was no municipal federal bankruptcy law at all. It wasn't really contemplated by the framers, and I'll get into that a little bit more in a minute, but what Bekins found was we now have this new federal municipal bankruptcy law. There is no state counterpart, so the only option that's available to the state

and the only way that the state can be accountable to its citizens to fix this problem if there is no other option available is to then consent to the federal court stepping in and doing this. Consistent with that, your Honor, we believe, is Asbury Park, and we would respectfully submit that Asbury Park was decided after Bekins. It was decided -- it wasn't a unanimous decision, but there was only one concurrence, so there was no dissent. It was drafted by Judge Frankfurter, hardly, you know, a slouch, and it specifically upheld Bekins but further found that a state -- in that case, New Jersey -- could correctly under its state municipal authority do a plan of adjustment that did not require 100 percent of consent, and in dealing with this issue, it found that to be consistent with Bekins because Bekins was looking at a situation where there was no state alternative for the state to choose, and the state only had one alternative, and it made the alternative to rely on the federal statute. And it further found -- and I'm going to quote just for a moment, Judge, but in dealing with this issue, the Court posed and then answered this very question. "Can it be that a power that was not recognized until 1938," which is a federal municipal bankruptcy law, "when so recognized, was carefully circumscribed to reserve full freedom" -- that's how Bekins interprets it -- "to the States has now been completely absorbed by the Federal Government -

that a State which, as in the case of New Jersey, has after long study devised elaborate machinery for the autonomous regulation of problems as peculiarly local as the fiscal management of its own household, is powerless in this field? We think not." And we think that's very telling, your Honor. And by the way, Asbury Park is still good law. Like Bekins, which it is consistent with, it has not been overruled, so the -- then we were grappling with, well, why hasn't anybody looked at this issue. What happened after Asbury Park was that the Bankruptcy Act incorporated a federal municipal bankruptcy statute, which is a predecessor to 903, which specifically includes a provision that provides, like 903, that no state can enter into a plan of adjustment unless there is a hundred percent consent. We find that interesting that it's the federal statute. Basically, that's Article -- that's Chapter 9 saying Chapter 9 is constitutional, and the states can't enter into an alternate separate plan of adjustment with less than a hundred percent because Chapter 9 says so. It's a circular argument, we would submit, your Honor, that can't possibly be the reason why the states can't enter into a plan of adjustment, especially in light of Asbury Park, with less than a hundred percent consent.

In addition to that, the other telling conclusion in Asbury Park was when they addressed head on the issue of the contract clause, they determined that the contract clause is

not violated when you don't actually violate the underlying contract. They were analogizing it to like the property rights, so while you have a contract right and that can't go away or you have a property right and that can't go away, what they were talking about in Asbury Park was what's the remedy, and the remedy in a Chapter 9 -- and we would respectfully submit the remedy in a state -- appropriate state plan of adjustment is to take what is now a valueless right -- contract right because the state municipality is insolvent and create a plan of adjustment that, like in the corporate bankruptcy setting, creates value for a right that had no value. We're not doing away with the contract, and a lot of the cases that come after that -- for example, United Trust that talks about taking away the bonds or changing the bonds -- Asbury Park says you're not taking away the contract, you're not taking away the bonds, you're not taking away our retiree benefits. All you're doing is you're saying, "Look, there's not enough money here to pay for it. We can't get it through taxation. We need to -- we need to fashion a remedy." And that, your Honor, we would respectfully submit is consistent with Bekins, with Asbury Park, and with an appropriate reading of the contract clause.

Turning now to the bankruptcy clause, there is a -- there is a provision that provides for a national bankruptcy statute. How can Chapter 9 be unconstitutional if we have

a -- if we have a bankruptcy clause that says there's a national uniform bankruptcy statute? Number one, we're directing our comments specifically at Chapter 9. We're not saying there is no statute that could be -- that could fit within the parameters. But that said, one of the things we would observe about the bankruptcy clause is when the framers framed the Constitution, it was inconceivable to them that there would be a national municipal bankruptcy law. To this day there is no national municipal bankruptcy law in the EU. And while Chapter 11 provides a very viable way to enable commerce and Chapter 7 provides a very viable way for there to be a fresh start -- and we've avoided debtor's prison and all of the things that the framers were focused on at the time -- there was no -- and there wasn't until the Great Depression a national municipal bankruptcy law.

Second, we think there's a problem with Chapter 9 specifically because the requirement of the national bankruptcy law is that it be uniform, so whether I'm here in Detroit or in any other state or city in the country, I know what the -- I know what the criteria is to be a corporate debtor. It's right in the Code. I know what the criteria is to be a Chapter 7 debtor. It's right in the Code. But because Chapter 9 is struggling with the difference of the separation of what's a federal power and what's a state power -- and we respectfully submit struggling in a way that

didn't work -- Chapter 9 is not a uniform statute. There are some states that have objective standards so that everybody in their particular state has to meet a certain criteria in order to be a Chapter 9 debtor. There are some states that don't even have the ability to be a Chapter 9 debtor, and then there are some states, like Michigan, where even though there's a statute that purports to authorize Chapter 9 filings, it is completely and totally subjective with regard to who qualifies, whether they get authorization to file, and whether or not there are any contingencies that are attached to what they do when they're in that filing.

THE COURT: Okay. So how do you distinguish the cases that uphold the nonuniformity of exemptions in Chapter 7?

MS. LEVINE: Your Honor, one of the -- two responses to that. First of all, we understand the case law that says that you can have conformity in a geographic location, so we understand, for example, that if every state had an objective standard the way every state has its own exemptions in Chapter 7, that that could meet the criteria for uniform standards, but we're saying something different. In Chapter 9 we don't know that every state has a standard or that they -- and if they don't have a -- and if they don't have a standard for becoming a Chapter 9 debtor, there is no default back to that which is provided under the Code. In other

words, in Chapter 7, if I like Detroit's exemptions, I use Detroit's exemptions. If I like the federal exemptions, I use the federal exemptions. But there is no place where I don't get to be a debtor or I don't get exemptions.

THE COURT: Well, but still the question remains how does a nonuniformity among states in authorizing or not authorizing Chapter 9 or in having different standards for seeking Chapter 9 protection make the federal law nonuniform?

MS. LEVINE: Well, your Honor, if you take that to its natural conclusion, you can say that I have a federal law that basically says you can do whatever you want, but because I'm saying you can do whatever you want to everybody, it's uniform. We would respectfully submit that that doesn't --

THE COURT: Isn't that just about what the Chapter 7 exemption cases say? Beyond that, federal law outside of Chapter 9 applies state property law, generally speaking, and, of course, the property law differs from state to state to state.

MS. LEVINE: Yes. And that goes back to the line of cases that talk about geographic, that they can be -- that they can be uniform within a geographic area. The difference between all of those cases -- and then I'll let the point rest because you are the Judge, and we may have to agree to disagree --

THE COURT: I'm just asking questions.

MS. LEVINE: But the -- but we view that, as I said earlier, that those exemptions, those criteria are published. Okay. So even if I know that I'm not going to follow -- that if I'm going to follow state law with regard to UCC priorities or if I'm going to follow state law with regard to exemptions, in a specific geographic area I know exactly what that is. In the states that have the subjective test with regard to whether or not to file a Chapter 9, Detroit has a different standard than Lansing and has a different standard than other cities, and that's the issue, and the issue -- and not only that, but none of those cities know what that standard is. And I'll leave it there.

THE COURT: Okay.

MS. LEVINE: Your Honor, the other argument that's out there is, well, doesn't the state have -- doesn't the state have the ability to cede control if there's federal aid. Your Honor, we would respectfully submit that's a very different situation. If you're looking at a situation, for example, like Sandy or like Katrina where the federal government is saying we're going to give you money under specific terms and conditions, that's different. Nobody is saying to Detroit or nobody is saying to every single Chapter 9 debtor if you file Chapter 9, you get "X" amount of money from the United States of America, and in exchange for that, you have to follow these certain rules. There's a difference

between entering into a contract for money and for support than ceding control just to do the plan of adjustment with no financial support.

THE COURT: Well, but the cases in which the Supreme Court has held the Tenth Amendment is violated by the federal government or the federal government's legislation involve what's called commandeering. Is there any of that here?

MS. LEVINE: Well, your Honor, we think that's -- we think that is, in part, what is happening here. The commandeering is they're taking away the state's right or the -- to do their own financial management.

THE COURT: But only because the state showed up.

MS. LEVINE: But that's not true, and this is where we go back to the Bekins --

THE COURT: Is there anything in Chapter 9 that compelled the state to authorize the city to file this case?

MS. LEVINE: Yes, and this is -- and this is where the argument comes. Okay. In Bekins there was no state alternative at all. In Asbury Park -- so, therefore, the Bekins Supreme Court made the decision that the state had no choice if it wanted to adjust its debt but to come to the -- but to come to the federal court. In Asbury Park there was a state alternative to the federal statute that was -- and that was permitted by both the federal statute and the state statute, so the arguments outside of the federal statute that

said you can't go to federal -- you can't do it statewide, you have to go to federal court under the commerce clause and otherwise, were rejected for some of the reasons that we're discussing here today. In Chapter 9 four year -- or the predecessor to Chapter 9, four years after Asbury Park, the Bankruptcy Code in its municipal statute said we can adjust debts at the federal level if you use the Bankruptcy Act, now the Bankruptcy Code, but you, states, cannot because of how we read the commerce clause only -- state municipal governments cannot adjust debt except with a hundred percent consent, so what the -- so what Chapter 9 says to the governor is if you want to do a plan of adjustment without a hundred percent consent, you must come to the federal government, number one. Number two, your Honor --

THE COURT: Well, but the commandeering cases address situations where the state and -- the federal government imposes on the state to carry out some federal program, some federal policy. How does that work here? So, for example, in the New York case, which involved the waste, right, nuclear waste or whatever, the state was forced to take title to it under certain circumstances, and the Court held that the state couldn't be imposed upon to do that to carry out the federal policy of how to dispose of this waste. How is that analogous here?

MS. LEVINE: Well, your Honor, the reason why we

believe it's analogous is because in order to do a plan of adjustment, arguably there's no other way to do that without using Chapter 9 unless you have a hundred percent consent, and that's the commandeering. The requirement that there be a hundred percent consent unless you're the federal government means that the state has no ability to do a plan of adjustment unless it cedes control to the federal government and to the bankruptcy process.

Your Honor, I'm coming up on time. If I -- unless your Honor has more questions, if I could just close briefly.

THE COURT: Well, the other question I have for you is what about the cases that hold that the lower courts are to apply Supreme Court precedent until the Supreme Court itself overrules it, and this is, of course, the Bekins case?

MS. LEVINE: Well, your Honor, our -- we would respectfully submit that Asbury Park was decided after Bekins. Right now where the Supreme Court sits is that Bekins stands for the proposition that in the face of no state alternative, which is what existed there, you can turn to the federal statute. Asbury Park stands for the proposition that side by side an appropriate municipal bankruptcy law and an appropriate state law, that's where the state gets to choose, and if the state, as it did in Asbury Park, chooses an appropriate state law that does permit for the adjustment of debt, then the state is accountable to its

citizens. If the state chooses the municipal law, then the state is accountable to its citizens. But either way, it's a true state decision. Consistent with both of those cases, we find ourselves here in Detroit with a situation where there is prohibited by Chapter 9, we believe unconstitutionally, no ability to have that second state decision.

THE COURT: Just so I understand, your argument is that the current Chapter 9 is different enough from Bekins because of its exclusivity that Bekins is not binding on this Court.

MS. LEVINE: Correct, and secondarily that Bekins never reached the issue because regardless of whether or not Bekins had an inappropriate -- the Bekins statute had an inappropriate clause, the state wasn't looking to have a separate -- you know, here we have PA 436 looking to try and pigeonhole itself into the strictures of Chapter 9 reviewing Chapter 9 as unconstitutional.

Your Honor, we believe your Honor is faced with a difficult decision here. We understand that Detroit is -- all that's happening here is difficult. Detroit is in dire financial straits, and it's not lost on any of us that the decisions that you make with regard to the criteria for eligibility, particularly with regard to Chapter 9, will have implications for blighted cities throughout the United States. We also understand that constitutional issues are

difficult issues. We heard -- you know, we've been grappling since 9/11, for example, with the balancing between homeland security and individual privacy rights. We started talking earlier about the First Amendment, and as a society we grapple between where does First Amendment end and where does a hate crime, for example, begin. This is no less an important constitutional issue because of the impact this will have on state sovereignty and the ability of its citizens to hold its own municipal leaders accountable.

Your Honor spent a long time listening to a lot of individual objectors here in this courtroom talk about how bad they felt things were in Detroit trying to deal with the fact that their firemen were using garden hoses, you know, street lights are out, all of these things, and your Honor was clearly sympathetic. And it was -- and concluded that hearing, we believe correctly so, by saying that this was a great day for democracy, but we would also add, your Honor, that despite the fact that these things are at the forefront of your mind and you want to do what's right, that doesn't necessarily mean that you can do what's expedious -- what's expedient. Democracy is hard, and we would respectfully ask that your Honor consider these issues with the same depth and consideration that you've considered everything in this case to date. Thank you.

THE COURT: Thank you. Mr. Montgomery also for 35

minutes.

MR. MONTGOMERY: Yes, sir. Thank you.

THE COURT: You may begin.

MR. MONTGOMERY: Good morning. Your Honor, my task today is to discuss with you constitutionality as applied, the standing and ripeness issue that the U.S. government has posed to our constitutionality as applied to argument, and to identify for you the predicate of that unconstitutionality as applied, which, of course, we believe is the unconstitutional behavior of Emergency Manager Orr and the governor in the context of PA 436.

I'd like to set the stage briefly for you, your Honor, on the question of standing by setting up two lines of -- view of history here. One is that in 1963 the State of Michigan amended its Constitution to protect the pensions of municipal workers. Partly in reliance on that protection, a small minority of the millions of people who have lived and worked in the city went to work directly for the city. Of those, thousands of people who worked, about 23,000 people are alive today who are retirees of the City of Detroit, their beneficiaries and surviving spouses.

Now, those 23,000 people have been, in our view, stalked by the emergency manager, who, with the blessing and support of his advisors, has proposed to eliminate pensions through a Chapter 9 process. On July 16th the emergency

manager sought permission from the governor to file a Chapter 9. On July 18 the governor, with full knowledge of the plans of his emergency manager, gave unconditional permission to the emergency manager to file that Chapter 9 petition. And the first overt harm has, in fact, now been announced. On October 11, the city mailed its books to the retirees announcing the termination of the retiree health insurance program for those same 23,000 people.

Now, the committee that I represent, your Honor, consists of nine individuals, including retirees, deferred vested, retirement eligible, surviving spouses and beneficiaries, all of whom are protected by the pension clause, all of whom are adversely affected by the harm that was just announced by the city. Each has or represents vested accrued pension benefits, and they are participants in the city's retirement health system.

The retiree committee consists of creditors appointed by the U.S. Trustee to act in connection with the case under 1102 and we think, therefore, have standing under 1109. Now, the 1109 standing of being an interested party may not be sufficient for either standing or ripeness on a constitutionality issue, but we say to you -- we ask your Honor to look at the current situation in the following analogy. When can somebody turn and defend themselves when they are being threatened with harm? We think that you don't

actually have to wait until the harm has befallen you if the threat is imminent, if the threat is capable of redress by the Court, and it is identifiable. The redress by the Court is, of course, denial of eligibility to the city. The threat is loss of pensions as announced by the emergency manager.

THE COURT: Of course, if eligibility is denied, the city is also denied its right to deal with all of its other debts, isn't it?

MR. MONTGOMERY: Your Honor, that may be a temporary delay because if your Honor holds that the current authorization papers are not constitutional or if accepted, despite their lack of constitutionality, the challenge to Chapter 9 becomes insurmountable, we think that the reasonable thing this Court could do if it were so inclined would be to deny the city its eligibility for the reasons of the challenge to the pension clause and then invite the city to come back with either a conditional acceptance by the governor or otherwise correct their manifest intent to violate Article IX, Section 24.

THE COURT: Well, what do I do if in Detroit two, as you propose, the bondholders come in waving the state contracts clause?

MR. MONTGOMERY: Well, your Honor, first, we think that there is a difference between Article IX, Section 24, and both the federal contracts impairments clause and the

state's own contracts impairment clause. We think that can be found in two places. First, there are extra words that can be found in Article IX, Section 24. In its entirety, Article IX, Section 24, has a phrase that appears at the end, which says "shall not be diminished or impaired thereby," the entire phrase, if I may, your Honor, "The accrued financial benefits of each pension plan and retirement system of the state and its political subdivisions shall be a contractual obligation thereof which shall not be diminished or impaired thereby," and, of course, your Honor, the second funding clause, which is, "Financial benefits arising on account of service rendered in each fiscal year shall be funded during such year and such funding shall not be used for financing unfunded accrued liabilities." Your Honor, that is, to my mind, certainly textually quite different than the state's own simple contract impairment clause, and we think meaningfully it's different. What Section -- Article IX, Section 24, does for -- in our view, your Honor, is tell the state that no matter what you are doing, you cannot take a step to adversely affect those accrued financial benefits, and we cite, of course, the Seitz case, which is the judicial probate case in which judges in the State of Michigan asked for protection of their pensions, and the Michigan Supreme Court agreed. We think it's also consistent with the Musselman case, which the Michigan Supreme Court said that,

again, the funding of retirement benefits that were otherwise protected or protectable had to be done, and the state could not take any action to not do that. Now, of course, that's a mandamus case in which the Court denied mandamus, but the legal proposition was squarely stated.

We also think the advisory opinions that the Court entered with respect to the tax exempt nature of retirement benefits clearly show that the Michigan Supreme Court looks to see if the state is doing something to impair the actual benefit. And that particular advisory opinion dealing with the tax exempt nature of retirement benefits, the Michigan Supreme Court said, no, merely taxing you or removing the special exemption is not an impairment of the financial benefit itself, so we step back and we ask your Honor to say, okay, is a plan proffered by the emergency manager with the knowledge and support or blessing of the governor authorized by a statute an unconstitutional series of events? Is the emergency manager's action unconstitutional, is the governor's action unconstitutional, or is the statute itself? Knowing that there is a judicial predilection for the narrowest possible reading of major problems, we submit to you that your Honor can start with the emergency manager's plan. Stop it. No eligibility if the emergency manager's plan is to be put forward. If that isn't enough because the governor authorized it, then you have to challenge the

governor.

THE COURT: Let me rewind the clock here just --

MR. MONTGOMERY: Sure.

THE COURT: -- a couple of minutes and ask you about this nonimpairment provision in the Constitution. The question we all are struggling with is what is the meaning, the substantive meaning of that provision in the context of a political subdivision that doesn't have the money to comply with it? What's the meaning of it?

MR. MONTGOMERY: First, I think this might be a good opportunity to agree with your Honor that impairment in the classic sense is something the Bankruptcy Code, of course, has dealt with for many years by saying the allocation of assets is not all by itself impairment. I think we -- I think it's fairly well established that just because a creditor gets less than a hundred cents does not mean that their contract is impaired. On the other hand --

THE COURT: I thought that's exactly what it meant.

MR. MONTGOMERY: That's if the state does it, but that's not that the -- remember the -- it was not a taking of property by the federal government to authorize the Bankruptcy Code. It was --

THE COURT: Oh, if that's what you mean --

MR. MONTGOMERY: Yes.

THE COURT: Absolutely.

MR. MONTGOMERY: Totally.

THE COURT: Absolutely, sure.

MR. MONTGOMERY: But it is a taking of property if the emergency manager says to its retirees, "I, either by virtue of a plan I put in or otherwise, am taking your right to receive pension benefits in the future," which is what he is proposing. He is not merely proposing to alter the funding system in violation of Article IX, Section 24. He is proposing to actually eliminate or reduce already accrued financial benefits.

THE COURT: Right, so what's -- how do we give meaning to nonimpairment, as you propose is constitutionally required, if the city doesn't have the money to pay? What does it -- what's the meaning of that requirement?

MR. MONTGOMERY: Well, your Honor, I think that if there is to be some allocation -- let's back up for half a moment. Let us assume for the moment that, in fact, the city has proposed to utilize all of its assets to deal with it, so we're not talking about a situation in which the city has capacity on its balance sheet or cash flows to deal with something that it just refuses to do. We think that the proper answer is not for the federal government to invite the state to violate its own Constitution but to have the state adjust its own laws, have the state, using its people, its either constitutional ratification process or the state

through its legislative process create the system for adjustments that Asbury Park tells us is still at least viable. Putting that aside, whether or not Asbury Park is or is not still --

THE COURT: Well, but hang on, Mr. Montgomery. If the pension right is as inviolate as you say it is, the legislature can't adjust the pensions either.

MR. MONTGOMERY: No, but it can adjust other people's assets, other people's entitlements. It can make the accommodations to its Constitution that may be required. It has the capacity to levy. It has the capacity to change property rights. The state legislature has those property -- and the only thing we are asking this Court to consider --

THE COURT: Well, let me ask this question then.

MR. MONTGOMERY: Yes, sir.

THE COURT: Is it your position that because of this nonimpairment requirement in the Michigan Constitution, the State of Michigan is a guarantor of retirees' pension rights?

MR. MONTGOMERY: We have not garnered nor do we propose to express a view today whether or not the state is a guarantor. What we are proposing to express a view today is that no state actor can do something in violation of the state Constitution and have that act be other than void ab initio. And if those acts are void ab initio, the requisite authorizations either don't exist or, if this Court has the

power to accept those authorizations notwithstanding their unconstitutionality under Michigan law, then your Honor is engaged not in aiding the sovereignty of the state, as suggested was required by Bekins, but you are aiding -- you are going in the direction of derogation of the sovereignty of the state. And why do I say that? Because you are telling the people of Michigan they can't control their own Constitution, they can't control their own legislature, they can't control their own executive officers, and we think that is a pure Tenth Amendment problem.

You mentioned earlier in discussion with Ms. Levine the commandeering issue. It is absolutely true, as you have identified, that first states must act in aid, not in derogation of sovereignty. That's the Bekins. Under Printz they can't compel a state official to do something that is otherwise the subject of a federal program. They can invite, they can entice, but they can't commandeer. That's the Printz -- that's the Brady Bill decision. And in the New York versus United States case, which, again, your Honor identified, you can't compel ownership of radioactive waste. Again, you can create programs, you can create enticements, you can create an exhaustive federal regulatory scheme that keeps the states out of regulating the business, but here the federal government can't, by virtue of the Tenth Amendment, keep the states out of regulating the financial obligations

of its citizens. It can't keep the states out of the business of deciding when their elected officials can or cannot do something, and it is that issue that causes the as applied problem as opposed to the facial and validity issues that were raised by AFSCME in the arguments of Ms. Levine. We think it --

THE COURT: I want to -- well, I want you to focus on why the mere filing of this case resulted in an imminent threat to the pension rights of the retirees of the city because the filing itself didn't result in anyone's payments being reduced; right?

MR. MONTGOMERY: Well, I will note for you they -- on the healthcare side, they apparently are.

THE COURT: Well, but that's not a result of the Chapter 9.

MR. MONTGOMERY: Well, actually, I don't think that could be done under state law because these are all collectively bargained -- or mostly collectively bargained, and to the extent they were collectively bargained, they're --

THE COURT: Well, but with or without the Chapter 9, Mr. Orr was free to do that or not under state law.

MR. MONTGOMERY: Or not under state law.

THE COURT: There's nothing about Chapter 9 that impacts his decision to do that. He hasn't asked, at least

as far as I know, the Court's permission to do that.

MR. MONTGOMERY: No. As far as we know, he hasn't asked either. So if I may answer the question, which, if I understood it correctly, was why is the mere filing --

THE COURT: An imminent injury.

MR. MONTGOMERY: -- an imminent threat, first, I go back to the factual predicate that I think underlays this, that the mere threat of filing -- excuse me -- the mere threat of a filing is not the harm all by itself, but it was preceded by an announced plan, the June 14 proposal, and a series of other events that the emergency manager undertook and statements made, which evidenced -- evidenced -- a desire to violate the state Constitution. Now, the only way in the emergency manager's own mind that he can do that is if he has access to the Bankruptcy Court because he believes it will trump the state constitution with respect to pension protections. Now, right or wrong, it is the -- it is the threat that those pension benefits will be eliminated as part of a plan, a series of steps of which have already been undertaken, the most recent of which was the filing of the Chapter 9 petition. The problem we face, at least in my view, your Honor, is that the world that you face today for deciding whether or not the emergency manager's actions are or are not constitutional under Michigan law is different in the eligibility context than we think you're going to be

faced with at a plan confirmation context. Once you're inside the box of bankruptcy -- excuse me -- everyone, putting aside whether -- how vigorously we will try to get state law to say something different, but everyone seems to suggest that the priority schemes and the allocation schemes of the Bankruptcy Code preclude a contrary result that would be allowable under state law.

THE COURT: Oh, but you're going to fight that.

MR. MONTGOMERY: But, your Honor, I've lost before, and I might lose again. The issue of --

THE COURT: Well, but if you lose, it will be on legal grounds.

MR. MONTGOMERY: But, your Honor, it will be. If we are fighting this issue at the back end of the case and we are arguing, as we will if we are required to, that notwithstanding 109, that the emergency manager can't propose a plan in good faith in which he violates his constitutional rights for --

THE COURT: Constitutional obligations, yeah.

MR. MONTGOMERY: Constitutional obligations. I apologize. For that to be a viable argument, in effect, you have to rule today, your Honor, that it would be a violation of his constitutional obligations because if it's not a violation in the context of adhering to the Bankruptcy Code provisions, which some cases say only provide with respect to

prospective obligations -- that is, a new pension plan would be subject to the protections -- well, we're not talking about a new pension plan, your Honor. We're talking about one that's been around for 60 or 70 years now, and we're talking about a retirement plan that has people who are a hundred years old.

THE COURT: Suppose the plan is confirmable because it results in the consent of those impaired after negotiation.

MR. MONTGOMERY: Your Honor, if our understanding of the law is correct, it's going to be very hard for a state official to agree in good faith to propose a plan that impairs financial benefits without a hundred percent of the retirees consenting either under 109 or under state law, and so the -- in order to get to the point where a less than 100-percent majority of the retirees are accepting the plan, you have to have decided that state law doesn't control the exercise of those rights.

THE COURT: Suppose you or one of your objecting colleagues decides to assert that the Michigan Constitution requires the state to guarantee the federal -- the retirees' pension.

MR. MONTGOMERY: Well, your Honor, the -- again, you are asking for advisory hypotheticals here, but --

THE COURT: Well, but that's what looking at

ripeness is all about.

MR. MONTGOMERY: The issue will be then not whether or not the bankruptcy process has harmed the retirees because it will have -- if the state is a guarantor or arguably a guarantor, it must be sued, query whether or not that lawsuit can be brought in the Bankruptcy Court or some other place, and, secondly, the -- under the Sittler case, I believe, there is a question of whether or not there's a cause of action for damages for unconstitutional behavior. There may be a remedy, an injunction against unconstitutional behavior, but the Michigan Supreme Court has not yet adopted a per se rule that says if there is a violation of the state Constitution --

THE COURT: Suppose the state agrees that the Constitution obligates it to guarantee the city's pension obligations.

MR. MONTGOMERY: Then the state will have remedied the harm caused by the bankruptcy, your Honor, but the harm was still being caused by the bankruptcy.

THE COURT: What harm?

MR. MONTGOMERY: The harm was the diminution of pension benefits.

THE COURT: Well, but if the state backs it up, there's no diminution.

MR. MONTGOMERY: Yeah. If, as part of a plan of

arrangement, the state backstops -- you're right, your Honor -- then the -- this is like a situation --

THE COURT: Okay. Okay. If I'm right about that, then why is the issue ripe now as opposed to then?

MR. MONTGOMERY: This is like the landlord case, if I may, your Honor, in which the -- I think it's Bennett versus City of San Jose, which, if I may, your Honor, since we didn't brief this issue, I can give you the cite for, but as I'm looking for the citation, I believe that case stands for the proposition that a landlord need not await the actual failure to collect more rent than he could under the new ordinance. He's allowed to challenge the ordinance when it's being passed. All right. We think this situation is very similar to that. We have a situation in which the emergency manager has undertaken an act, has sought the aid of this Court, and the question is do we have to wait for this Court to, in effect, put it to us before --

THE COURT: No, no. The question isn't that. The question is do you have to wait for the emergency manager to actually propose a plan that impairs pensions -- that's the question -- and then object to that on constitutional grounds.

MR. MONTGOMERY: In the Thomas More Law Center case, your Honor, the -- which is the commerce clause challenge to minimum coverage provisions under the Affordable Care Act,

three and a half years in advance, the Sixth Circuit found standing because notwithstanding the fact that it was a long way off and many things could occur, including Congress changing the law, different rules being applied, that was enough because there was nothing the party asserting the claim had to do in order to become injured. Now, yes, there were things that any member of the law center group could do that could escape the harm, but the fact that they had to undertake affirmative steps to escape the harm was enough.

Here the only thing we can do to escape the harm which the emergency manager has announced he will undertake is to escape, and the only way to escape is through the gates that your Honor is standing at the door of. You are the keeper of the protection for the retirees. You are the one who can stop the emergency manager from doing what is unconstitutional under Michigan law. And apparently, by the way, both the state and the city are inviting you to rule on constitutionality issues, you know. They are perfectly comfortable with your going down that road, your Honor, and notwithstanding our hesitancy --

THE COURT: Does that make an otherwise not ripe issue ripe?

MR. MONTGOMERY: No, obviously not, your Honor, but we do think that where there's -- where the voluntary cessation by the city or the temporary cessation or the

temporary abandonment of its statements that, oh, we are going to impair the pensions does not create a situation that moots the controversy nor do we think it eliminates the ripeness of the controversy because your Honor can still see the identifiable harm and can still issue an order that redresses that identifiable harm by telling the city it may not enter the portals of your courtroom.

Now, your Honor, I think we have, in effect, distinguished the Barnwell case, which is cited by, I believe, the U.S. government, because that was an ad hoc committee of citizens instead of an 1102 committee. Here we're clearly creditors. Here 1109 grants us statutory standing as parties of interest, and I think we have indicated to you that the harm is factual, imminent, and you are at the gates.

One other thing I might want to sort of identify in this ripeness issue, why now as opposed to what, why later, of course, your Honor is familiar with the City of Stockton case, and we are not urging you to adopt that case obviously, but it does suggest that once in Chapter 11, the State of California couldn't decide which rules it was going to follow.

THE COURT: Chapter 9?

MR. MONTGOMERY: Right, in Chapter 9, the same thing your Honor might decide here; that is, once inside Chapter 9,

the city is not free to do whatever it wants to do except with respect to its own property and its own future governance. That you cannot touch in any way, shape, or form, but that doesn't mean that you have to approve a plan that violates what your Honor thinks are the rules of the road. And it is that danger that you would be called upon to make a ruling inconsistent with Michigan law at the back end of the case that has us asking you at the front end of the case to prevent the city from engaging in that dialogue.

Now, the -- I think worth making as a final, if you will, point -- and, again, later this afternoon you will hear a more fulsome discussion, I believe, on all of the issues associated with PA 436, but I think the void ab initio issue is important to our constitutionality position; that is, were it not for the fact that under Michigan law an unconstitutional act is considered void ab initio, we think you might be able to go down the road of accepting the authorization papers as having been legitimately delivered to your Honor without fear of violating our view of how Chapter 9 would be unconstitutional as applied; that is, if Michigan law did not regard unconstitutional acts as void ab initio, then all you would be faced with is a remediable situation rather than an absence of action or an absence of authorization action. And with respect to the void ab initio cases, we have cited those in our brief, your Honor, and we

think that you should accept as a truism, if you will, the simple words actually uttered by Attorney General Schuette in his paper that the city lacks authority under Michigan law to propose a plan that diminishes accrued pension rights. It similarly lacks power to consent to any proposed action that would violate the Michigan Constitution. The proposed action was the petition. The proposed action was the petition as part of a plan to eliminate the pension rights induced -- the emergency manager got the governor to say yes to an act that was unquestionably contrary to the pension clause. As a void ab initio act, that means that the legitimacy of the filing is called into question, pure question of state law for your Honor to rule upon, pure question of whether or not, in fact, the city has obtained valid authorization papers -- pretty hard to be valid if the underlying actions are void ab initio, which is the norm under Michigan law, and we think, therefore, your Honor has two ways to go down the path of blocking eligibility independently of the factual disputes under 109. One is to hold that it's unconstitutional, the authorization was unconstitutional because it was part of a scheme to eliminate the pension rights or to say even if it wasn't void ab initio, the acceptance of those actions by this Court raise a huge constitutional challenge under the Tenth Amendment to Chapter 9 itself. Obviously the principle of limiting federal constitutionality challenges would favor

finding that the narrower ground would be that the emergency manager couldn't have filed his papers. And I think, your Honor, just because I must, I just want to argue we are not arguing -- we are not rearguing today all those issues which we were in front of your Honor before several weeks ago about Stern v. Marshall and whether or not the Court should do that. We are in front of you. You have determined that you have the power to decide issues of state and federal constitutionality. We are asking you to exercise that power and to preclude the city's eligibility.

THE COURT: So if you don't -- we have a little time left. I have some more questions for you.

MR. MONTGOMERY: Sure. Happy to engage, your Honor.

THE COURT: One is sort of a procedural one. You mentioned that you didn't brief the ripeness issue. Would you like an opportunity to do that?

MR. MONTGOMERY: That would be fine, your Honor.

THE COURT: I'd leave it to your discretion.

MR. MONTGOMERY: Yes, yes.

THE COURT: How much time --

MR. MONTGOMERY: We'd be happy to do that, your Honor.

THE COURT: How much time would you like?

MR. MONTGOMERY: Give us a week, your Honor.

THE COURT: Okay. You have a --

MR. MONTGOMERY: Yeah. Give us a week. It'll be -- if you don't mind, we'll submit it to you on the first day of the trial.

THE COURT: Okay. I want to ask you about a couple of entries in the brief that you did file.

MR. MONTGOMERY: Okay.

THE COURT: On page 27, you say -- and I want to quote here. This is the brief you filed at Docket Number 805.

MR. MONTGOMERY: Yes.

THE COURT: You say, "As noted by the Sixth Circuit in City of Pontiac Retired Employees Association, 213 Westlaw 4038528 at *1-2, the Michigan legislature evidenced an unconstitutional, and undemocratic purpose in crafting PA 436," close quote. Similarly, on page 29 of that brief you say, "The Michigan legislature, the Governor, and the Emergency Manager have each made clear that abrogation of municipal retirement compensation rights was the legislative intent of the Act," referring to PA 436, "and is a central purpose of this bankruptcy. That intent also was recently recognized by the 6th Circuit in City of Pontiac Retired Employees Association," same cite at *3. I have to say, Mr. Montgomery, that I have studied that opinion by the Sixth Circuit several times, and I cannot find these references. I cannot find where the Sixth Circuit addressed or even

suggested anything about the constitutionality of PA 436. Am I missing something or was this a mistake?

MR. MONTGOMERY: Well, unless my memory fails me, your Honor, I think what we're referring to is the fact that the Sixth Circuit said that PA 4, which was the immediate predecessor of 436, had each of those purposes, your Honor, and that, therefore, by extension --

THE COURT: Perhaps so, but the Court didn't say anything about PA 436.

MR. MONTGOMERY: Well, other than that it was adopted despite the fact that the referendum had overruled PA 4 and that it was virtually the same but for -- I believe the phrase was an add-on for --

THE COURT: The Sixth Circuit did not say anything about the purpose or intent of PA 436.

MR. MONTGOMERY: But it did as to 4, your Honor.

THE COURT: It did.

MR. MONTGOMERY: And it says 4 -- 436 is the same as 4. That's how we got there. Rightly or wrongly, that is how we got there, your Honor. We say if the Sixth Circuit identified a purpose of PA 4 as being the impairment of pension --

THE COURT: Well, since you're going to file an amended brief --

MR. MONTGOMERY: Yes, sir.

THE COURT: -- I want you to tell me very specifically where in this City of Pontiac case the Court said anything or suggested anything about the constitutionality of PA 436.

MR. MONTGOMERY: All right. Your Honor, we will --

THE COURT: I agree with you it addressed it at length with regard to PA 4 and expressed grave concerns about it, but that's not the act before this Court today, so I invite you to do that in your --

MR. MONTGOMERY: Of course.

THE COURT: -- new brief.

MR. MONTGOMERY: We'll add that discussion to our ripeness supplemental brief.

THE COURT: All right. Thank you.

MR. MONTGOMERY: Thank you, your Honor.

THE COURT: Ms. Brimer, you may proceed for ten minutes, please.

MS. BRIMER: Thank you, your Honor. Lynn M. Brimer appearing on behalf of the Retired Detroit Police Members Association. Your Honor, your concluding arguments or discussion with Mr. Montgomery leads directly into the discussion that I will have with you this morning, and that has to do with the constitutionality of PA 436 under the Michigan Constitution, your Honor. And first and foremost, your Honor, I'd like to point out that in our brief we

noted -- and we cited the Schimmel case -- we noted that PA 436 was passed in what we believe is derogation of the Michigan referendum provision in Article II, Section 9, of the Michigan Constitution. It is well worth noting at the outset of this discussion, your Honor, that that issue was not addressed by either the city or the State of Michigan in the pleadings they have filed.

With that, your Honor -- and I'll address that a bit briefly later, your Honor. Article I, Section 1, of the Michigan Constitution specifically provides that, "All political power is inherent in the people. Government is instituted for their equal benefit, security and protection." Consistent with that maxim, Article II, Section 9, of the Constitution specifically provides -- and it's a lengthy provision, your Honor, so I'll read the relevant provisions -- "The people reserve to themselves the power to propose laws and to enact and reject laws, called the initiative, and the power to approve or reject laws enacted by the legislature, called the referendum. The power of the referendum does not extend to acts making appropriations for state institutions or to meet deficiencies in state funds." As has been noted, your Honor, in a handful of cases that we can find that address this case, this provision of referendum is so significant and vital to our Constitution that Article II, Section 9, further provides that, "No law as to which the

power of referendum properly has been invoked shall be effective thereafter unless approved by a majority of the electors voting thereon at the next general election."

As this Court is aware, I'm sure, on November 6, 2012, by referendum, the people of the State of Michigan rejected Public Act 4 on a vote of 52 to 48 percent. That was the Local Government and School District Act -- Accountability Act. On December 26, Governor Snyder approved Public Act 436, the Local Financial Stability and Choice Act, a virtually identical law to Public Act 4.

In order to avoid subjecting Public Act 436 to referendum, two very minor spending provisions were tacked on at the back end. Section 34 of the Act provides that for the fiscal year ending 9-30, 2013, $780,000 is appropriated to administer the Act, in essence, to pay the salaries of the emergency managers appointed thereunder, and Section 35 provides that $5 million is appropriated for the same time frame for the professionals such as lawyers and financial consultants that are engaged under the Act. The spending provision was not at all a general spending provision for the State of Michigan but a very limited provision relating directly to the Act.

We have researched, your Honor, and cannot find a single instance where the voters of Michigan have specifically rejected a law and shortly thereafter the

governor passes a very similar law, if not identical, and tacked on a spending provision in an effort to remove it from the otherwise democratic process of the State of Michigan.

There are a handful of cases in Michigan that do address the referendum. In the case of Kuhn v. Department of Treasury at 384 Mich. 378, 1971, the Michigan Supreme Court specifically provided or held that the phrase in the preamble of that -- the Income Tax Act of 1967, which provides that the Act is for the purpose of meeting deficiencies in state funds was not, in fact, sufficient when at the time the state did not have any state deficiencies in its funding, and, therefore, that provision in the preamble did not, in fact, remove the Income Tax Act of 1967 from the power of referendum. Unfortunately, in that case the plaintiff had not complied with the requirements for referring the matter to the -- or the law to the referendum, and so the Court was not able to render any further opinion regarding that language and its impact on the -- whether or not that case had -- that law had it been brought to referendum. However, it's instructive to this Court. The law at issue in that case had not previously been rejected on referendum, so, therefore, it does have some influence in how this Court should interpret how the Michigan Supreme Court may view the two spending provisions tacked onto Public Act 436. Public Act 4 had, in fact, been rejected by the state through a

proper referendum. The spending provisions were added on in an effort to remove the case -- the law from the referendum in derogation of the provision in Article II, Section 9, which provides specifically that no law to which the power of referendum had been properly applied shall be effective thereafter unless approved by a majority of the electors voting thereon at the next general election.

THE COURT: Okay. So I have this question for you regarding this argument, and it's, again, a ripeness question and a standing question. How does any party have standing to challenge the constitutionality of PA 436 on this ground or why is it ripe until such a party has complied with all of the legal requirements to have a referendum regarding that put on the ballot and it being rejected because the law isn't subject to a referendum because of this appropriations provision?

MS. BRIMER: I don't believe, your Honor, that by adding on the spending provision, which on its face took Public Act 436 out of the referendum provision of the statute -- if that is the case, your Honor, then you have read out the referendum from the Michigan Constitution. I think this is precisely the mechanism by which the constitutionality of the law now should be challenged. When that law was then relied upon for purposes of the appointment of an emergency manager, that is precisely, I believe, your

Honor, how this would come to a court for review. On its face, the governor attempted to remove this from the referendum. It was removed from the referendum, but you can't read that out of the law and read out of the Constitution the second provision, which requires that any law that has been rejected by referendum be resubmitted to the electorate.

I see I'm running out of time, your Honor. What I would like to note, your Honor, is that while you are correct that the Sixth Circuit did not specifically rule on 436 -- I've read that case closely several times -- 436 was not before the Court, and, as you'll recall, some of the matters at issue in that case were what precisely is before the Court because some of the arguments had not even been preserved on appeal. However, I think the tone of the Sixth Circuit when it said, "Apparently unaffected that voters had just rejected Public Act 4, the Michigan Legislature enacted, and the Michigan governor signed, Public Act 436. Act 436 largely reenacted the provisions of Public Act 4, the law the Michigan citizens had just revoked. In enacting 436, the Michigan Legislature included a minor appropriations provision, apparently" -- they didn't say "in fact," but "apparently to stop Michigan voters from putting Public Act 436 to a referendum." I think that gives us a tone, and I also think it's noteworthy, your Honor, that despite the fact

that the city noted on page 15 of Exhibit A to their consolidated response to the objections that we had raised this specific issue, it is not addressed. It is not responded to by either the state or the city. It stands unrefuted at this point, your Honor.

THE COURT: Thank you.

MR. GOLDBERG: Good morning, your Honor. Jerome Goldberg appearing on behalf of interested party David Sole, who is a city retiree, as is his wife, Joyce Sole.

THE COURT: And you may proceed for ten minutes, sir.

MR. GOLDBERG: Thank you, your Honor. While I certainly concur with many of the eloquent arguments put forth by counsel prior to myself, I want to approach the issue from a somewhat narrower point of view from the prism of Michigan state law and specifically from the Michigan -- how Michigan state law views the issue of statutory construction.

As we know, 11 U.S.C. 109 states that a local municipality must be specifically authorized by state law to file a Chapter 9 bankruptcy. The phrase "authorized by law" refers to the law of the state, and I cited Bekins for that principle. States act as gatekeepers to their municipalities and access to relief under the Bankruptcy Code.

As we all know, the basis for the state law

authorizing the filing of this Chapter 9 is Public Act 436, and Public Act 436 has several different provisions that I think it's worth looking at to get an understanding for why we believe the failure to include a contingency to bar the impairment of pensions is violative of state law. It provides the emergency -- Section 1551(c) provides the emergency manager with the power to carry out the modification, rejection, termination, and renegotiation of contracts. Section 1552 provides the emergency manager again with the power to reject, modify, or terminate, one, terms of an existing contract. Section K gives the emergency manager the power to reject, modify, or terminate an existing collective bargaining agreement. Section 12 contains provisions for the renegotiation of debt, and it's laid out in Section 12. But what Section 1552(m) -- Section 12(m), when it deals with the question of pensions, it explicitly includes within the section, within the statute, the -- states that the emergency manager must fully comply with Article IX, Section 24, of the Michigan Constitution, which is the constitutional prohibition on diminishing or impairing contract. In addition, Section 1558 states that the governor may place contingencies on a local government in order to proceed.

When you view the statute -- the authorizing statute from the prism of the Michigan rules on statutory

construction -- and I cited the Pohutski case, which many -- is the seminal case on statutory construction in the State of Michigan, Pohutski -- the Michigan Supreme Court in Pohutski stated, "When parsing a statute, we presume every word is used for a purpose. As far as possible, we give effect to every clause and sentence. 'The Court may not assume that the Legislature inadvertently made use of one word or phrase instead of another.' Similarly, we would take care to avoid a construction that renders any part of the statute surplusage or nugatory." And, in addition, Michigan courts follow the doctrine of expression unius exclusion alterius, the expression of one thing is the exclusion of another.

We would submit that in construing Public Act 436 as a whole, in construing it as a whole, any -- you can't allow for the filing of a Chapter 9 unless the Chapter 9 includes the contingency for not impairing the pension rights under Article 24. Otherwise it would negate that section or declare that section void, and that would be an express violation of the Michigan Rules of Statutory Construction, which the Court is bound to follow at this stage in the proceeding because in the eligibility proceeding, it is state law, state law that is dominant. We believe, based on --

THE COURT: But aren't there many, many, many conditions that the governor could have put on the filing in order to assure the emergency manager's compliance with state

law?

MR. GOLDBERG: There are certainly different --

THE COURT: Equal protection, due process of law, freedom of speech.

MR. GOLDBERG: But what I'm submitting, your Honor --

THE COURT: There are lots of constitutional rights.

MR. GOLDBERG: Certainly. But what I'm submitting is we have to look at the statute as it is written. That's what the Michigan courts rule over and over again. Those are the fundamental rules of statutory construction enunciated by the Michigan Supreme Court in case after case. In this case, we look at the words of the statute. We don't read into the statute. We look at the words of the statute. This statute contains an explicit guarantee of pensions, a guarantee --

THE COURT: Well, and the governor says --

MR. GOLDBERG: It includes Article IX.

THE COURT: The governor says the filing will comply with state law, doesn't he?

MR. GOLDBERG: Well, the governor may say it, but the governor is not the final arbiter, your Honor. That's what the Court is for, and what we -- and the governor is not above the law.

THE COURT: Why isn't that a sufficient protection?

MR. GOLDBERG: I'm sorry.

THE COURT: Why isn't that a specific -- a sufficient protection?

MR. GOLDBERG: Why isn't what the governor says a --

THE COURT: No. Why isn't the fact that this Court will apply state law a sufficient protection?

MR. GOLDBERG: Well, we would submit, your Honor, that state law at this stage of the proceeding, at the authorization stage, is the determinative factor. Once we go into the -- once you make the eligibility determination, as Mr. Montgomery indicated and as the case law as I've read it indicates as well, that's where federal law -- there's a question of federal supremacy over state law, but at this stage it's state law that is determinative, and the state law in this case explicitly mandates a contingency for the guaranteeing of pensions. Otherwise we've written that section --

THE COURT: If we're going --

MR. GOLDBERG: -- out of the authorization statute --

THE COURT: If we're going to look at --

MR. GOLDBERG: -- and that's an explicit violation of statutory construction.

THE COURT: If we're going to look at statutory law and every word of it, how do you deal with the city's argument that the word "thereby" in the constitutional

provision only prohibits the impairment of pensions by the state or its political subdivisions; it does not prohibit the impairment of pensions by a United States Bankruptcy Court?

MR. GOLDBERG: That's exactly the point, your Honor. That's exactly the point. At this stage of the proceeding, according to Bekins, according to Harrisburg, and according to every case I've read, according to Collier's, it's state law that is determinative. That's why --

THE COURT: And that's what I'm asking.

MR. GOLDBERG: That's why the question --

THE COURT: And that's exactly what I'm asking you about. If we're going to read every word of the statute and apply every word of the statute, including the word "thereby," why doesn't state law permit the Bankruptcy Court to impair pensions?

MR. GOLDBERG: Because the authorization statute that this Court is relying upon, which it has to rely upon because otherwise there would be no Chapter 9 filing, there has to be a specific authorization under state law; correct? I mean there are 20 -- many states don't have one. You have to rely on the state law. That state law contains an explicit clause that impair -- pensions cannot be impaired. It's not just written in one place actually. It's written in two places in that statute. Again, I'm submitting that down the road, if we get past this eligibility question on this,

perhaps what you said is correct. At that point federal law -- you make the determination based on federal law, but right now you are duty bound to make that determination based on your examination of state law and by applying the state law --

THE COURT: What is the --

MR. GOLDBERG: -- principles of statutory construction.

THE COURT: What is the exact state law language in PA 436 that you rely on?

MR. GOLDBERG: I rely on the language -- here, let me find it right here.

THE COURT: Okay.

MR. GOLDBERG: "The emergency manager shall fully comply with the public employee retirement system investment act and Section 24 of Article IX of the state Constitution, and any actions taken shall be consistent with the pension's qualified status"; that he's -- this emergency manager has to abide by the constitutional impairment.

THE COURT: So my question for you remains if this Bankruptcy Court were to approve a plan -- and I want to say here I have no predisposition on this issue at all. This is strictly hypothetical legal talk to figure out where we are. If this Court were to approve a plan that impairs pensions -- again, not presuming at all that it will -- but if it did, is

that the city impairing pensions, or is that the Bankruptcy Court impairing pensions because --

MR. GOLDBERG: That would be impairing --

THE COURT: -- the law prohibits the city from doing it? There's a question about whether it prohibits the Bankruptcy Court from doing it.

MR. GOLDBERG: That's precisely why I'm making the argument, your Honor. There is a -- there is a question as to whether -- once we get past the eligibility and this Court is looking at the plan, whether this Court then has the authority under federal law to ignore the state law and state constitutional protection. I'm not saying it does, but there's at least a question, and a lot of the case law indicates that, but we're not at that stage right now. We're at the eligibility stage, and clearly at the eligibility stage it's state law that predominates. It's state law that's determinative, and it's state law that this Court has to look at, not federal law but state law that this Court has to look at in making its determination as to whether the authorization meets the muster. And what I would submit, that under state law principles, as I indicated, we look at the authorization statute, we look at the plain language of the statute, and we look at the Michigan rules on statutory construction as a -- and there's no way to allow for a filing that would not have a contingency that bars the impairment of

pensions. It's interesting to me you raised before to Mr. Montgomery --

THE COURT: Actually, your time has expired, so I do have to ask you to wrap up.

MR. GOLDBERG: Okay. Well, I'll make one last point. You raised very briefly to Mr. Montgomery why not every contract, but, as I indicated, other contracts are provided for the impairment of those contracts under the PA 436. It's the impairment of pensions that's explicitly taken away from the authority of the emergency manager, and I submit because of that that any authorization that doesn't include a contingency barring the impairment of pensions would violate Michigan state law and violate the Bankruptcy Code, in essence, itself. Thank you.

THE COURT: Thank you.

MS. CRITTENDON: Good morning, your Honor. Krystal Crittendon, and I want to thank the Court for giving me the opportunity to speak this morning.

THE COURT: Welcome, and you may proceed for five minutes.

MS. CRITTENDON: Thank you, your Honor. Before the Court goes any further, I would just ask that the Court step back and look at the process and how we got to where we are from a legal foundational standpoint, and to that end, I make three objections, your Honor.

First, the City of Detroit does not have a duly appointed emergency manager because there was no EM or EFM law in place at the time that appointment was made. As the Court knows, in 2011, Public Act 4, commonly known as the Emergency Manager Act, repealed Public Act 72. In November of 2012, the people of the State of Michigan repealed Public Act 4 by referendum. Pursuant to Michigan law -- and this is at MCL, Michigan Compiled Law, 8.4 -- "Whenever a statute, or any part thereof shall be repealed by a subsequent statute, such statute, or any part thereof, so repealed, shall not be revived by the repeal of such subsequent repealing statute." In short, that is saying that when PA 4 repealed Public Act 72 and PA 4 was then repealed by referendum, PA 72 was not revived. It did not spring back to life.

On March 14, 2013, a contract was purportedly entered into between the State of Michigan and Kevyn Orr appointing him EFM for the City of Detroit. However -- under PA 72. However, because PA 72 was not alive at that time, that appointment was not legal and is defective, and for that reason, Mr. Orr is not a duly appointed emergency manager for the City of Detroit.

The second argument, even had there been an emergency manager law in place, Mr. Orr would not have been an EFM at the time PA 436 came into place because his contract, the contract between he and the state, was expired

on the day that PA 436 came into place, so he would not have been grandfathered in under PA 436.

Finally, under Chapter 9 of the Bankruptcy Code, there is no ability for there to be an involuntary bankruptcy, and because the municipality would had to have filed the petition, and in this case the municipality, being the mayor and City Council, did not file the petition, the petition filed by Mr. Orr was defective, and the filing should be dismissed.

For those reasons -- and I see that my yellow light is on -- time goes really really quickly when you have five minutes, but I'd answer any questions the Court has.

THE COURT: Hoe much time is left when the yellow goes on, Kelli? Do you know?

THE CLERK: Three minutes.

THE COURT: It's three minutes, so you only --

MS. CRITTENDON: Okay.

THE COURT: -- had two under green and three under the yellow, so --

MS. CRITTENDON: Okay. Thank you, your Honor.

THE COURT: -- you may proceed.

MS. CRITTENDON: Mr. Orr's contract at Section 2.2 of that contract provides that his contract was effective on Monday, March 25th, and terminated at midnight on Wednesday, March 27th. Midnight March 27th was a Wednesday morning at

12 o'clock a.m. The new emergency manager law, PA 436, did not take place -- did not become effective until Thursday, March 28th. Under 14 -- MCL 141.1572, it provides that an emergency manager or emergency financial manager appointed and serving under state law immediately prior to the effective date of this Act shall continue under this Act as an emergency manager for the local government. Because the City of Detroit was without an emergency manager or emergency financial manager for one full day before the Emergency Manager Act, PA 436, became effective, Mr. Orr could not continue in that capacity, as used in this section, because he was without a contract.

Finally, I would just say there are a number of cases under the federal Bankruptcy Court law that talk about involuntary bankruptcies. This is akin to an involuntary bankruptcy when someone other than the City of Detroit, which is its mayor and City Council, filed the petition. And for those reasons, the petition was defective. Section 109 of the Bankruptcy Code talks to the authorization of the state to approve a bankruptcy if filed by a municipality. In this case, that is not what happened. It was the state effectively filing the petition and approving the petition being that the emergency financial manager, assuming that we had one, would be an operative of the state and not an operative of the City of Detroit. Thank you, your Honor.

THE COURT: Is the contract on which you rely in the record of the case?

MS. CRITTENDON: I don't believe it is. I do have a copy of the contract with me if the Court would like to see it. I'm assuming that one of the parties --

THE COURT: If you'd like me to consider it, you should --

MS. CRITTENDON: I will file it.

THE COURT: -- file it.

MS. CRITTENDON: I will, and I will file a brief that memorializes everything that was said today.

THE COURT: All right.

MS. CRITTENDON: Thank you, your Honor.

MR. MORRIS: Good morning, your Honor. Thomas Morris on behalf of the Retiree Association parties. The Retiree Association parties who I represent include two individuals. There was some discussion about the committee's standing to raise certain objections. The committee argued those objections very ably. We concur in those objections, and that includes the concurrence of those individuals. We trust that would take care of any standing issue if there were one. And the comments that preceded us -- preceded me were very ably made, so I'm just going to address a very few points.

One is a point the Court -- a question the Court had

raised about the "thereby" language in the pensions clause. It's important for the Court to note that it's the city that files any plan, the city that proposes any plan, negotiates any plan. Chapter 9 precludes the Court from appointing a trustee, from converting the case, from interfering with the city's ability to manage its fiscal affairs. A case cannot be filed involuntarily under Chapter 9. As the Bekins court said, quoting from the legislative history on page 51, "The taxing agency itself is the only instrumentality which can seek the benefits of the proposed legislation." We think it's clear that any action to impair the pensions by the city would, first of all, be improper, but, second of all, it would be the city's action.

Now, the city has taken the position that somehow the pensions clause of the Michigan Constitution is preempted, and we disagree with that, but the city can't have it both ways. They have a theory -- they've made a number of multiple arguments, but they have a theory that once they got into Bankruptcy Court -- or if they get -- are found eligible, then the pensions clause is off. Well, if that's the case -- and it's not the case, but if that were the case, then it would be the action of the authorization of the filing and the action of the city in filing the case which would be impairing the pensions. What happens if the city is found ineligible?

THE COURT: Well, but that's true only if as part of eligibility the Court ruled on the issue of pension rights and ruled in the city's favor.

MR. MORRIS: This ties in with arguments that were made by other counsel, and if Public Act 436 enables the city to impair the pensions, then Public Act 436 in that respect is unconstitutional. It's inconsistent with the pensions clause. Of course, the pensions clause is part of the Michigan Constitution, the supreme law of our state, and the Public Act 436 must comply with it. Public Act 436, in fact, gives recognition to the pension clause and acknowledges it, and it even authorizes the governor to make compliance with the pension clause a precondition. However, that didn't happen in this case, and that's one of the -- one of the issues that has been raised by other counsel.

Your Honor, if the city is found to be ineligible, from the standpoint of the retirees, the city will have to make a choice. It can choose to comply with the pensions clause and not impair pensions, just say we're going to comply with the Michigan Constitution, or it can negotiate with the retirees through their associations. That process was shortcut here, and that will be one of the factual issues we've raised.

Now, if the city goes forward with a plan that does not impair pensions, one of the Court -- one of the questions

the Court had was what happens then, what happens if the city just doesn't have the money. Well, there's an issue of whether the state is liable. There's the potential issue. But those are all issues apart from -- they're nonlegal issues. The most the retirees can ask for is that the city doesn't impair the pensions. The ultimate solution for the retirees comes elsewhere. Will the city have -- will the state have to step in to help the city? Will the city have to do other things to raise money? I don't know, but those are beyond our legal issues.

Your Honor, the city holds the key on this issue of eligibility. It can agree to comply with the Michigan Constitution or it can negotiate with the retirees and reach a resolution. The proper outcome here is for the city to go back -- as Section 109 intends, go back and either not impair the pensions, which is our preference, or negotiate with the retirees. Thank you.

THE COURT: Thank you.

MS. FLUKER: Good morning, your Honor. Vanessa Fluker on behalf of Center for Community Justice and Advocacy.

THE COURT: Would you repeat your name for me, please?

MS. FLUKER: Vanessa Fluker.

THE COURT: Okay. Thank you.

MS. FLUKER: F-l-u-k-e-r. Your Honor, the issue I'm raising today before this Court with respect to eligibility is a failure of the emergency manager to comply with the statutory mandates under PA 436, Section 16, which is actually Section 1556. That section specifically mandates, and I quote, "an emergency manager shall," not "may," not "might, "shall, on his own -- his or her own or upon the advice of the local inspector if a local inspector has been retained, make a determination as to whether possible criminal conduct contributed to the financial situation resulting in the local government's receivership status. If the emergency manager determines that there is a reason to believe criminal conduct has occurred, the manager shall refer the matter to the attorney general or local prosecuting attorney for investigation." There has been some extensive arguments about the tenets of statutory construction, so I won't go through Pohutski step by step, but we're all aware that you must adhere to the plain unambiguous language of the statute.

In this particular instance, two of the city's largest creditors, UBS and Bank of America, have been found convicted -- criminally convicted in UBS's case of criminal conduct involving municipal bonds. In fact, the SEC fined UBS $47,207,180 in Case Number 11-2539, U.S. District Court, New Jersey. Three UBS executives were indicted and convicted

of fraud related to municipal bond rigging, and that was in New York, Southern Division, Case Number 10-1217. A Bank of America executive was indicted July 19th, 2012, for bid rigging of fraud municipal bonds. And what's so significant about this, in the criminal conviction with the SEC case, the civil penancy case, it involved a Detroit bond. This provision cannot be ignored, and the mere fact that it's mandatory because it indicates "shall" is very significant. In fact, it is common knowledge at this point that the emergency manager had knowledge of this information and did not act on it. In his deposition on August 30th, 2013, he was specifically asked on these issues,

"Are you aware of issues that have come out with regard to the LIBOR specifically with UBS and Bank of America in the setting of using the LIBOR as a standard?

Answer: I am aware.

Question: Are you aware that UBS has been sued by the Securities and Exchange Commission for rigging in regard to municipal bonds?

In past years?

There was a final judgment -- yes, in past years.

Answer: Yes. I've heard that. I have not read the final judgment.

Question: Are you aware that Bank of America has been investigated for potential bond rigging with regard to the municipal bond market?

Answer: I am aware that Bank of America has been investigated. The exact specifics of the investigation I am not aware of."

This clearly shows that there is not just a noncompliance with 1556, there's a knowing noncompliance with 1556. There should have been a criminal investigation, which is mandated by the statute, and, in essence, is necessary to even get to the point of making a recommendation for a bankruptcy. How can you say that we need bankruptcy when you don't know whether there is going to be fraud determined and there may be funds that may be necessary to be paid back to the city that can offset any debt, which also goes to the issue of how are you saying that you're eligible for bankruptcy when you really don't know what the debt is based on the potentiality of fraud in these municipal bond transactions, who are also standing --

THE COURT: Are you saying that the emergency manager, whose term in office is limited by law, was required to await what could be years of litigation to determine these issues and UBS's liability before filing bankruptcy?

MS. FLUKER: I don't think he had to determine years of litigation, but I think that it would be very evident that

you would look at least at the debt that you're alleging that the city owes, and if there is common knowledge of such information, which this is -- this is not something that you have to wait years in litigation. This has been all over the news, the Internet, and everything else. And as he admitted in his deposition, he was aware of it, and that being the case, that actually heightens the duty, in addition to the mandatory language of Section 1556, which says "shall."

THE COURT: Shall do what?

MS. FLUKER: The statute specifically says the emergency manager shall, on his or her own or upon the advice of a local inspector, make a determination -- there had to be a determination made -- whether there was criminal conduct that affected the financial situation of the city. Even if he didn't know all this, say for some reason this information -- I see my time is up. I'll just complete this sentence. Say this information he had no knowledge of. There was -- we just don't know about it. He still had a duty to make a determination. Well, in my estimation, there's been no criminal conduct that contributed to the financial situation of the city. This provision was not complied with at all, and you cannot try to exercise one part of the statute by totally ignoring and having noncompliance with another. Therefore, I would request that this Honorable Court deny eligibility for the reasons set forth by all the

objectors.

THE COURT: Thank you.

MS. FLUKER: Thank you.

THE COURT: Mr. Gordon, may I have your attention, please?

MR. GORDON: Yes, your Honor.

THE COURT: Are you up next?

MR. GORDON: I am.

THE COURT: Okay. Do you want to give part of your argument now, or do you want to take a lunch break now and then do your entire argument after lunch? I leave it to you.

MR. GORDON: If it's okay with the Court, I would prefer the latter, to just start after lunch.

THE COURT: Okay. All right. We will take our lunch break now, and we will reconvene in an hour and a half, so that'll be 1:20, please. Twenty after one we'll reconvene.

MR. GORDON: Thank you, your Honor.

THE CLERK: All rise. Court is in recess.

(Recess at 11:48 a.m., until 1:20 p.m.)

THE CLERK: Court is in session. Please be seated. Recalling Case Number 13-53846, City of Detroit, Michigan.

THE COURT: Good afternoon, everyone. It looks like everybody is here. Actually, Mr. Gordon, with your permission, before I hear from you, I have a follow-up

question for one of your colleagues.

MR. GORDON: By all means, your Honor.

THE COURT: Ms. Brimer, would you resume the lectern, please?

MS. BRIMER: Should I bring something with me, your Honor?

THE COURT: Possibly.

MS. BRIMER: I didn't know I was going to the principal's office.

THE COURT: No, no, no. It's nothing like that. You argued that the enactment of PA 436 violated the people's referendum rights because PA 436 was so similar to PA 4.

MS. BRIMER: Yes, your Honor.

THE COURT: That was your argument. Was there a statutory basis for that argument, or was it just based on the people's right of referendum?

MS. BRIMER: It's based on the constitutional right of referendum, your Honor.

THE COURT: Okay. So there's not a statute we should be looking for on that.

MS. BRIMER: Not that I'm aware of, your Honor.

THE COURT: All right. That was it.

MS. BRIMER: Thank you, your Honor.

THE COURT: That was it. Okay. Mr. Gordon.

MR. GORDON: Thank you, your Honor. Just to give

your Honor a little bit of a road map of the things that I want to touch upon, if that's of help, I thought I would touch upon some of the issues regarding the state law consent, some of the issues that have been raised this morning, then move on to a discussion of some other considerations relevant to the difference between the pensions clause and the contract clause, and then address the issue of what would happen if the Court ruled in our favor that the accrued pension benefits cannot be impaired and what that means for the restructuring, and I think I can add some important information there. And then finally, if there's still time, I would touch upon the collateral estoppel Webster issue, which is in our papers.

So, your Honor, we will start with the consent issues under 109(c)(2), and to be clear, in our papers, while we talk -- touch upon the possibility of PA 436 being unconstitutional as applied, the thrust of our papers is that PA 436 needs to be read and can be read in a way that's consistent with the pensions clause and so forth so that there's no need to get to issues of constitutionality. 109(c)(2) clearly is an issue that is an issue purely of state law. It is a threshold issue. It is an eligibility issue, and we want to emphasize that it stands on its own, and it can't be conflated with plan confirmation issues.

THE COURT: And with apologies, I have to stop you

there with this question. There seems to be a general thread of assumption that whether a state has given authorization under 109(c)(2) is a question of state law, as you just said. I have to say that's not altogether clear to me. It seems to me there might very well be an argument that the standard as to whether the state has given proper authorization is a federal standard, not a state standard. Why? Because in addressing cases in the amendment right next door to Article X -- that is, Article XI -- sorry -- Amendment XI, the 11th Amendment, when we talk about sovereign immunity, the issue of whether a state has given its consent or its waiver of sovereign immunity is a question to be determined by federal law, not state law.

MR. GORDON: Your Honor, in that regard, I think that the Tenth Amendment is different, and it looks first to respect the contours of what is reserved to the states in the first instance, so here I think you have to start with whether there is valid -- I think, at a minimum, the question is is there valid state authorization for submitting a political subdivision of the state to the jurisdiction of the federal government and the federal courts. I would at least put it that way. And so that does turn on state law, and we would submit that all portions of state law need to be looked to and harmonized in that regard, and that's sort of the holding of Harrisburg, which we submit is instructive here

and which has not been really in any way refuted by the city. And even the United States Attorney has stated that Congress reserved to the state the right to regulate, and I quote, "under what terms," end quote, its political subdivisions may avail themselves of Chapter 9, so it really is a matter, I believe, of state sovereignty, and it's up to the state to determine how and when a political subdivision can avail itself, and how it does that is in part expressed by the will of the people, as embodied in the pension clause, and it needs to be respected.

The response of the city and the state is on two levels. One, first of all, it is asserted that the actions of the governor in authorizing do not conflict with the pensions clause because the authorization itself didn't create any impairment and that it's unclear whether the city will ultimately seek to impair, and if such impairment occurs, it won't be the city or the state that has done it. It'll be the Bankruptcy Court. Respectfully, we say that those arguments are all unavailing. First of all, one of the things that I think has not been made clear this morning is some of the things that have come out in discovery. I don't actually think these things are relevant, but I'll get to why I think they're not relevant in a minute, but I think it's important for the Court to know that in discovery propounded by the Retirement Systems or conducted by the Retirement

Systems, the city has admitted that it was an explicit intent in the restructuring plan proposed in June and in the bankruptcy recommendation letter submitted on July 16th by Mr. Orr that accrued pension benefits needed to be impaired. The city has also admitted in admissions that its intent in the Chapter 9 case is to impair and diminish accrued pension benefits, so there is absolutely nothing speculative about that. The governor has also testified that he was aware that accrued pension benefits may be impaired. He also testified that he understood that he could put conditions on the consent and authorization and that he chose not to. Mr. Orr also testified that he could not guarantee that if a consensual plan couldn't be achieved, that he would not resort to cramdown provisions in order to cram down upon the retirees. So there really is nothing speculative here, and for anyone to say that it is speculative is really -- I mean it just is not -- it's just not factual.

THE COURT: Well, but what would be the --

MR. GORDON: The other thing is that --

THE COURT: What would be the impact on that argument if the state, under this Constitution, does have a legal constitutional obligation to guarantee the pension payments, an issue not yet determined? And I don't mean to suggest the outcome of that by raising this possibility.

MR. GORDON: Your Honor, I mean if the -- the

problem is that today is the day for eligibility, and we don't know that today. If the state came forward today and said that they would backstop, you know, the full accrued pension benefits, that might be a different situation, but it not being here today, that isn't --

THE COURT: And you're not prepared to say here today that you're not going to request that conclusion, are you?

MR. GORDON: No. I will not say that, but that's --

THE COURT: That would not be in your client's best interest.

MR. GORDON: Of course not. Of course not, but that has not been determined today. The state is not coming forward today. And eligibility goes to whether this Court even has jurisdiction, and what the city is asking is for the Court to essentially suspend the issue of whether it even has jurisdiction in order to get everybody together, and really you're putting the will of the people and the protections of the Michigan Constitution in jeopardy or being held in the hold while the city wants to move forward with its proposals and bring people to the table, and I would submit that that's inappropriate. This is an eligibility hearing, and the governor's responsibility is an affirmative responsibility to uphold the Constitution. To suggest that we don't know what's going to happen down the road reduces his obligation

to sort of a wink and nod type of standard, and we submit that that is just inappropriate. He is to uphold the people's will.

THE COURT: Well, he's to uphold the law.

MR. GORDON: The other thing is, your Honor, that to say that someone other than the state or the emergency manager would be the one impairing the benefits is just not correct. As the Court well knows, the city is the one that would have to propose the plan. The Court would not propose the plan. Essentially what is happening here would be that the governor, through the authorization, is delegating authority that he does not have. He does not have the authority to abrogate the state Constitution. By authorizing the emergency manager to pursue the bankruptcy -- again, we're at the eligibility stage -- he cannot give authority to the emergency manager that he does not have, so the question becomes --

THE COURT: The argument is he doesn't have the authority to impair the pensions.

MR. GORDON: That's correct. If he wanted to do that, he'd have to go get a constitutional amendment.

THE COURT: And -- okay.

MR. GORDON: So he does not have the authority to delegate or to bestow upon anybody else the ability to impair, so the question really is why wouldn't we put a

condition today saying that you can move forward in the Chapter 9, but you can't impair the accrued pension benefits? That to us complies with the requirements of the state structure, and there has absolutely been no explanation of why that wouldn't be done today. We think that's the real question is why wouldn't you -- why wouldn't the governor put that condition in or why can't the Court imply that as a matter of law?

If I may, your Honor, I'd like to move on to the pensions versus contracts issue.

THE COURT: Well, hold on one second. The Sixth Circuit has actually addressed -- I know you're concerned about time --

MR. GORDON: Okay.

THE COURT: -- the issue of how to determine eligibility in bankruptcy, now not in Chapter 9, but it did so in Chapter 13 because there is a factual eligibility issue there, has to do with debt limits, and there are times when creditors say that the debtor's debts are above the debt limits, and, therefore, the debtor is not eligible, so the Sixth Circuit -- the case is Pearson if you're familiar with it. It says -- it recognizes that at the eligibility stage of a bankruptcy, you don't want to go through the process of fixing claims, but there is this law that sets debt limits, so we have to give it some respect. So the solution it came

up with in that context was we're just going to look at whether the debtor in good faith asserts that its debts are below the debt limit. And for those of you who want it, it's 773 F.2d 751, 773 F.2d 751, a 1985 case from the Sixth Circuit. Pearson is P-e-a-r-s-o-n. Why not apply a similar standard to eligibility here?

MR. GORDON: Because there's no good faith issue here. The question is very simple and can be solved today. Are you going to impair pension -- accrued pension obligations? You can't. The law says so. So put the condition on it today, and we move forward.

THE COURT: So your assertion is that it wouldn't even be a good faith argument by the city.

MR. GORDON: Doesn't matter what their intention actually is. The condition should be applied today because that is how -- that is the only way a --

THE COURT: It wouldn't be a good faith --

MR. GORDON: -- political subdivision can avail itself --

THE COURT: It wouldn't be a good faith argument for the city to assert that although the Michigan Constitution prohibits it from impairing pensions, it does not prohibit the Bankruptcy Court from impairing pensions. That would not be a good faith argument?

MR. GORDON: No, your Honor. I think that that's

something that can and should be dealt with today. Let me give an example. What if the only debts of the city today -- as we stand here today were pension obligations? Would you say then we should wait and see what happens? We know what would happen. Is it any different because there's other creditors in the room?

THE COURT: Well, do we know --

MR. GORDON: I haven't --

THE COURT: Do we know -- do we know what would happen? Do we know, for example, that there would be no agreed upon negotiation? Do we know, for example, that the state won't fill in the gap?

MR. GORDON: Well, let's -- I can talk about that.

THE COURT: Now would be the time.

MR. GORDON: If you want to talk about that, I'll skip to that. I'll skip to that since that seems to be something that is troubling your Honor or at least on your mind. We have emphasized --

THE COURT: A question.

MR. GORDON: We have emphasized that the Retirement Systems aren't saying the city can't proceed with a Chapter 9 case. It simply must condition the case upon the preservation of the pensions clause. And certainly in some people's minds this begs the question of whether in the event the Court agreed and ruled that accrued pension benefits may

not be impaired, could the city still effectively reorganize and restore itself to financial health through a bankruptcy, and while we've indicated that there is still information that we need -- and it's material information -- we continue to do so -- I believe I can stand here today and say that based upon the information that we do have, it is clear that the city can effectively reorganize even if accrued pension benefits cannot be impaired.

Just some thoughts and facts for your Honor. The city talks about $18 billion in debt, but $6 billion of that $18 billion is special revenues that are supported by the Detroit Water and Sewer System, so now you really have $12 billion of debt that needs to be supported by the general fund and other cash flows from the enterprise funds and so forth. Of that $12 billion of debt, roughly half, six billion, is OPEB healthcare actuarially calculated. Another two billion is unsecured bond debt. So fully two-thirds of the $12 billion of debt is very much subject to restructuring and compromise in bankruptcy. Those are unsecured claims. That's two-thirds of the $12 billion of debt right there. So there's a tremendous opportunity to unburden the city of the debt obligations -- of these debt obligations and the demands on its cash flow.

In addition, although not critical to this position, above the line in the emergency manager's restructuring plan

proposed in June is the swap periodic payment, which is soaking up $50 million a year in casino tax revenues. And as the Court knows -- and, again, I'm not going to argue it here, but, as the Court knows, the Retirement Systems have objected to the treatment of the swaps as secured in those revenues both because the lien is not valid and, even if valid, it does not reach the post-petition revenues. Also -- and if it was determined to be an unsecured claim, then you have a $300 million claim now that is given unsecured status and can also be a compromise in the bankruptcy.

Also, it should be kept in mind that we're talking about accrued benefits that need to not be impaired. There are obviously prospective benefits that could be impaired, so there are a number of different ways that the city can achieve real relief from its debts. Obviously it spreads the pain in different directions, but we've -- but by looking at it, your Honor, there is absolutely an opportunity to do something. And when they --

THE COURT: Isn't there also a question of fact as to what the underfunded liability is for pensions?

MR. GORDON: And let me get to that. It's also critical for the Court to understand that if the Court ruled in our favor and said that there cannot be an impairment of the accrued benefits, that does not mean the Retirement Systems walk away from the table. The Retirement Systems has

said that they are committed to working with the city to be part of the solution here. That means a number of things. The city has indicated that it needs to devote significant cash flows in the next five years, according to the proposal in June, $1.25 billion in the next five years for reinvestment in the city. The Retirement Systems don't object to the concept and understand that the city needs to reinvest, but after that five years, that reinvestment is done. The cash flows of the city become much larger again, and they will improve at five years and the next five years and the next five years. And the Retirement Systems can be flexible because the Retirement Systems issues, the pension issues, are long-term issues. They're not short-term issues. So if there are cash flow issues, the Retirement Systems can work with that. The $3-1/2 billion number that's been thrown out there is not an amount that is due today if the pension systems are not frozen and closed. That is an actuarial calculation of what will be due over the next 30 years to bring the funding level up to what it needs to be. That's not the amount that is due on a cash flow basis tomorrow or the next day, so there is flexibility there.

Also, it should be understood that over time if the economy improves or interest rates rise, and/or, the underfunding level may go up or down, so there's a lot of things in play there, and when you take that all together,

we --

THE COURT: And I certainly appreciate and commend your clients' willingness to work with the city, but prudentially from the standpoint of ripeness apart from constitutional issues, doesn't that suggest putting off until plan confirmation the issue of the constitutional right?

MR. GORDON: Your Honor, again, I would submit that that is conflating eligibility, which is one question, with what can be done under a plan. If this Court does not have jurisdiction because the authorization was not appropriate, if you're putting -- what you're suggesting -- or the city is suggesting is you're putting the uncertainty -- you're putting at risk a state protected benefit in order to leverage people to get in a room and negotiate. And I suggest, as a matter of jurisprudence, that is inappropriate.

I wanted to also mention, your Honor, other benefits of a ruling in favor of the concept that the pension benefits cannot be impaired. It, in fact, would help the city in its restructuring in other ways. Absent a ruling on this issue in favor of the nonimpairment of pension benefits, the parties will struggle to negotiate in the shadows of this unresolved issue. What will happen is that the parties will have to negotiate on a dual path against the backdrop of still having these arguments under the pensions clause, under Section 943, and so forth that are all or nothing arguments

that would -- if ruled on in a certain way, would come to the conclusion that you can't impair us at all. So it makes the negotiations very difficult, and it also obviously -- as long as that matter is not resolved or if it's not resolved in favor of the pension systems, it becomes -- it makes the case much more litigious and encumbers the entire process. If the Court rules in our favor -- and, again, these are just, you know, some additional thoughts for the Court because I understand the struggle. If the Court rules in our favor, there will be less moving parts for the city to deal with and for the parties to deal with, and it makes the negotiation process much more streamlined. And if at some point in time that decision were reversed and there was a decision that said that the pension clause can be abrogated or impaired in some fashion, having to revise the negotiations at that point and spread the pain around a different way is a lot easier than starting from the other end. If you start from the end that we're at now, it's very hard, again, for the parties to negotiate. And if the -- and if it's determined ultimately that you can't abrogate the pension clause, then you're really going back to square one, and we've lost a ton of time in the negotiation process. We submit that it's much easier to negotiate against a backdrop that says that the pension clause must be upheld.

Moreover, a ruling in our favor in that regard helps

the city in other ways. It calms the workforce knowing the accrued and prospective accrued pension benefits will be protected. This will enable the city to retain its most talented personnel. In addition, the ultimate commitment of funds to the Retirement Systems as opposed to financial creditors benefits the city because the systems will also invest in the city, as they always have done. And a majority of the pensioners live within the city and pay taxes and consume goods and services in the city, so the Retirement Systems are an economic engine that really is part of the solution for the city, so I want to address all those.

THE COURT: Well, but so were the bondholders and the bond investors.

MR. GORDON: They don't live in the city, and they aren't putting money back into the city, your Honor. They are not part of that economic engine, and if they get paid their debt service, there's no --

THE COURT: Hang on.

MR. GORDON: -- guarantee that they're going to reinvest in the city.

THE COURT: Didn't I read in the newspaper that the city just got $350 million?

MR. GORDON: I'm sorry.

THE COURT: Didn't I just read in the newspaper that the city just got $350 million to help with its reinvestment?

MR. GORDON: No, your Honor. What we read was that there's a proposal to secure unidentified assets at this point but probably to encumber all sorts of assets of the city in order to get $350 million of which 200 million would immediately go out to pay swap participants who don't deserve to get paid anything as a secured creditor, and then the other 150 million is going to be used in some ways that's been unidentified, so basically you're encumbering assets of the city for purposes that don't benefit the city in any demonstrable way at this time, so I would disagree with that characterization.

THE COURT: Okay.

MR. GORDON: So, your Honor, for all those reasons, I think that if the Court were to rule, again, as a pragmatic matter, in favor of finding that this case should not move forward without the condition that there cannot be an impairment and that the pension clause must be upheld, it does not mean this case comes to an end by a long -- quite the opposite. In our opinion, it makes this case much more manageable. It makes the negotiations easier. And it, in our minds, provides a much clearer path to a consensual resolution.

THE COURT: So you think I can find them eligible and find that pensions can't be impaired? How do I do that because the issue is yes or no, the city is eligible.

MR. GORDON: That's correct, your Honor. You would have to -- it would be up to the city to either -- and the state to either agree to -- well, there's a couple different ways.

THE COURT: This is the refiling scenario?

MR. GORDON: You could either -- you could either rule that the obligation to uphold the pension clause is implied by law because otherwise you don't have valid authorization, there isn't valid state authorization, or you can provide the option to the state and the city to explicitly confirm that process.

THE COURT: Oh, I see. So you're saying I can read into the authorization the nonimpairment of pensions even though the governor explicitly rejected that.

MR. GORDON: The governor actually didn't. The governor testified that he didn't know whether he had to uphold that, and he decided to choose not to put the condition on it and leave it to the courts, which we suggest is not necessarily appropriate but is --

THE COURT: So he rejected the concept of conditioning his authorization on nonimpairment of pensions.

MR. GORDON: He did, but he also said he was basically deferring to the courts as to how that should play out, which is ironic because the Webster court has already ruled on that issue.

Your Honor, I'll turn to the pensions clause, which is the contracts clause, if I may.

THE COURT: Sure.

MR. GORDON: The concept that the pensions clause is the same thing as the contracts clause just applying to pensions does violence to the language of the pensions clause, as has already been discussed.

THE COURT: Right.

MR. GORDON: I won't get into that. Obviously we've pointed out that the pensions clause is more specific and that it was enacted long after the contracts clause and that those things together, as a matter of the canons of construction, would indicate that the pension clause must mean something more and something different from the contracts clause.

THE COURT: Right. So what more and what different?

MR. GORDON: Well, it starts with looking at why and the environment in which these things were done and looking at the actual language of the two clauses. The contracts clause was adopted back when the government was being formed, and it helps sort of support the structure of the government as it's being developed in terms of federalism and making sure that states don't impair their -- pass laws that impair their own contracts or pass laws that favor their citizens over other citizens. That was the general nature of it. And

it's directed, you'll note, to the legislature of the state. The state shall not pass laws that will impair contracts. So that's the contracts clause. Now you fast forward --

THE COURT: That's the federal contracts clause.

MR. GORDON: And the state, as well as the state contracts clause. So then you fast forward -- I don't know how long -- 150 years to 1963, and you're talking about the constitutional convention and the pensions clause, and what's going on at that point in time? Well, pensions are not being funded. They're underfunded across the state I'm told to the tune of maybe $600 million, and guess what? Front and center is the City of Detroit that was not paying pensions for its teachers' pensions funds. So the convention decided it needed to do two things.

THE COURT: Well, at that point they were also not being treated as contracts; right? They were being treated as gifts I think was the phraseology.

MR. GORDON: As gratuities. That's correct, your Honor. So the convention decided it needed to do two things. The convention decided, first of all, to avoid municipalities digging a deeper hole, they were going to put a provision in the Constitution that said that local governmental units will fund their current year's employer contributions in that year to help avoid digging a deeper hole. Secondly, to protect the accrued and unfunded liabilities and to move away from

the concept that they are a gratuity, the convention said we're going to call it a contract but not a contract in the sense of a contract but subject to the bankruptcy. I mean there was no -- there was no talk about bankruptcy, nor was there any talk about the contracts clause in this regard. They talked about this is going to be a contract that's in the concept of a solemn binding obligation that will be paid over time, so it is a contract. There's a contractual right, and it shall not be diminished or impaired, meaning it will be paid over time by the state and its political subdivisions. It is absolute. There is no -- there is no -- as the attorney general's papers say themselves, there is -- it's impermeable unlike the contracts clause, which has developed over time to say otherwise. Now, the difference is in part --

THE COURT: But how can the -- how can the state contract -- how can the state promise that given that under the federal Constitution it can't print money?

MR. GORDON: It's a matter of insuring that what dollars are available are devoted where they need to be devoted.

THE COURT: Suppose there's not enough then.

MR. GORDON: I don't know the answer to that question, your Honor, but that's not the issue we have here today. As I've told you, I think that there is enough money

here.

THE COURT: It's an important issue.

MR. GORDON: There is -- I'm sorry.

THE COURT: It is an important issue.

MR. GORDON: It's an important issue, but --

THE COURT: It demonstrates that there's a constitutional right there. It is stated there, but what's it worth? What's it worth? I mean Ms. Levine posed that question. What's it worth if the entity that has the obligation doesn't have the means?

MR. GORDON: First of all, I mean every situation is different.

THE COURT: Yeah.

MR. GORDON: Does it have the means today or will it have the means tomorrow, over time? Musselman, a state Supreme Court case, says, though, that the pension clause cannot be abrogated in the face of financial exigency. That's what it says. If there's a need to amend the state Constitution, then it needs to be amended, but it can't be abrogated by one branch of the government. The will of the people has spoken. The Constitution is a limit, and it circumscribes the power of the government. The government can't say, "Gee, we've got an exigency here. I guess we're going to ignore the state Constitution." It cannot do that. The contracts clause is different, and this is the point --

part of the point is there are contracts and then there are contracts.

THE COURT: Is there any other constitutional right, state or federal, that is that absolute, any other?

MR. GORDON: Sure.

THE COURT: And even freedom of the press has its exceptions.

MR. GORDON: Well, you know, if you look at even the attorney general's papers, you couldn't -- the legislature can't pass laws that would abrogate freedom of religion, freedom of speech, things of that nature, and it puts the pension clause on the same level. It is absolute in that regard. There are contracts, and there are --

THE COURT: We have laws that limit speech. Can't threaten the President; can't yell "fire" in a crowded theater. You can't commit libel.

MR. GORDON: So that maybe there's some regulation on the federal level, but this is a state issue. It is an issue that has been -- it is the will of the people of the state.

THE COURT: Even the contracts clause has its limits; right?

MR. GORDON: Contracts clause does. The reason is different, though. There are contracts, and then there are contracts. And if you look at, for example, you know, some

contracts fall under the contracts clause, but the pensions were determined to be different, and that's why you have a pensions clause. That's the whole point of it. The contracts clause recognizes that when you contract with the government, there is an inherent reserve police power to act in the public's welfare, and, therefore, to the extent necessary, in certain situations they can impair contracts. That's the contracts clause. Then you have the pensions clause. It doesn't say that it is subject to the contracts clause. It elevates pensions to a different level, and the reason is fairly clear. If you look at the Musselman case, in particular, again, Musselman says that Michigan governmental -- and I quote. This is from 448 Mich. 503 where it talks about the pension clause being absolute and that it -- and it recognizes that the pension clause protects pensions for work performed, so I quote, "Michigan governmental units do not have the option, however, of not paying retirement benefits. Unlike highway construction or police protection, which a governmental unit can choose to receive less of, it is impossible to receive less service from the pensioner. The pension payment is payment for work already completed, or deferred compensation," end quote. What's being referenced there is the complete difference -- the relationship between the public employer and labor is different than the relationship between the public employer

and a bondholder. A bondholder makes an investment. There's risk involved. That is understood, and that risk is factored into the pricing of the bond. A laborer has -- the relationship with the employer is different. The laborer works. The employer pays. And to the extent that part of it is deferred compensation in the form of a pension, so be it, but it's for -- but what the pension clause protects is accrued benefits.

THE COURT: Isn't there an argument that labor takes risks with its employer, too?

MR. GORDON: Not in the State of Michigan, your Honor, and I want to emphasize that. Michigan is only one of seven or eight states in the country that has this clause. This is unique to Michigan and the seven or eight other states involved.

THE COURT: Excuse me one second. I want you to ignore --

MR. GORDON: Oh.

THE COURT: No. I want you to ignore that yellow. My staff advises me that Ms. Levine didn't use seven of her minutes, so I'm going to yield them to you.

MR. GORDON: Thanks, Sharon.

THE COURT: So reset the clock at ten. I assume that's okay with you.

MR. GORDON: Yes, absolutely, your Honor. I can't

even remember where we were now. Where were we?

THE COURT: Oh, I'm sorry. I interrupted your train of thought. Well, take another minute to recollect --

MR. GORDON: Oh, yes. I think I finished that point, I suppose. It really is that, you know, some contract rights are just contract rights, and other contract rights do rise to the level of property rights, and that's in the United States Trust Company of New York versus New Jersey, the Supreme Court case, 431 U.S. 1. In Michigan AFT Michigan versus Michigan, 297 Mich. App. 597, the Court held that withheld salary of public school employees constituted the taking of property in violation of substantive due process and the takings clause, so there are relationships, contractual relationships relative to accrued benefits for labor, pension obligations, that are treated as property.

THE COURT: Is there a State of Michigan case that holds that pension rights are property rights?

MR. GORDON: Well, this relates to salary of public school employees. I don't know --

THE COURT: Right. So I was asking you about pensions.

MR. GORDON: About pension obligations specifically? I would have to check on that, your Honor, but I believe that there are pension cases in the state that talk about pension rights as property, including in such a situation, as you can

imagine, as divorce settlements. There are pension obligations that become property that get part of a property settlement even, but that's just one example, but I can get you --

THE COURT: Well, we have to be careful here because a contract right is in the bundle of property rights. Every contract is property of the parties to the contract; right?

MR. GORDON: Yes, your Honor. I'm not sure that all contract rights rise to the level if they're abrogated of a taking, but here vis-a-vis the pension --

THE COURT: Right. That's exactly the point.

MR. GORDON: That's right, but the pension clause --

THE COURT: So when the federal, you know, Bankruptcy Court discharges creditors' contract rights against debtors, which we do all day every day, we're not taking the creditors' property rights even though we are discharging those contracts or if we are it's not a Fifth Amendment violation; right?

MR. GORDON: True. By the same token, there are other property rights that are determined under state law that -- cases such as Butner and Travelers respect the state law property interest, and it flows through the bankruptcy.

THE COURT: Right, but the point is that it has to be a property right under state law over and above what would be the contract right, like, for example, a security

interest.

MR. GORDON: Or a state constitutionally protected right that is impermeable we would submit, your Honor.

THE COURT: Okay.

MR. GORDON: It's like a nondischargeable debt, your Honor, and it doesn't mean that it can't be dealt with in a way that doesn't impair it but gets dealt with in a way that is -- you know, provides some flexibility for the reorganizing entity, but it's a nondischargeable debt.

THE COURT: Well, nothing in Chapter 9 provides for any nondischargeable debts, is there?

MR. GORDON: I'm stating it by analogy, your Honor, obviously.

THE COURT: Okay. All right.

MR. GORDON: By putting the condition on that you can't impair, it becomes a nondischargeable debt essentially, and the state has that authority to place the appropriate conditions on the filing of the bankruptcy to protect the statutory structure. And it's not just statute. I mean this is -- the difference here again, this is really unique. It's not like California or Alabama.

THE COURT: Hypothetically, a state legislature passes a law authorizing municipalities to file Chapter 9 so long as the plan provide -- the municipality's plan provides for a priority of payment, and it turns out that that

priority of payment legislatively required by the state legislature is different from the Bankruptcy Code. Let's assume that. Would it be your position that no municipality could file Chapter 9 in that case because the state law contravenes the superior -- or the supreme federal law?

MR. GORDON: Well, that's an interesting question because it sounds more like one of those situations where once you're in bankruptcy, you have to accept the structure of the Bankruptcy Code itself, and that highlights --

THE COURT: That's exactly what the city is arguing here.

MR. GORDON: And that highlights the point here that eligibility has to be dealt with at the eligibility stage and that -- and to put off the question of whether you can impair the pension clause leads to those vagaries of questions about, "Well, now we're in bankruptcy. Does the Bankruptcy Code have vitality and in what regard?" No. You don't get to those questions unless you have valid state authorization. You don't have valid state authorization unless you've taken into account what provisions need to be there to protect the state Constitution and other statutes, and that's sort of what Harrisburg talks about. You may have facial authority under one statute, but you got to look at the other statutes. And in here in this case it's --

THE COURT: So in my hypothetical you would say

there's no valid authorization.

MR. GORDON: I would say that the state may be very disappointed if it authorizes and allows the debtor into bankruptcy only to find that the -- that part of the protection goes away.

THE COURT: It's hard for me to be concerned about how the state feels. Is it your position that there would be no authorization, no proper authorization in that case?

MR. GORDON: Let me understand the hypothetical then. I know time is short. The hypothetical is that the state would pass a statute that says that you can file Chapter 9, but the priority of payments is going to be --

THE COURT: But here are the priorities. Here are the priorities. You got to pay bonds first, and, you know, you got to pay --

MR. GORDON: Perish the thought.

THE COURT: Sorry?

MR. GORDON: Perish the thought, but go ahead.

THE COURT: Okay. Perish the thought all you like, but this is the hypo.

MR. GORDON: Yes.

THE COURT: You got to -- you pay the bonds first, and you got to pay trades, and then you got to pay employees' wages, and then you pay pensioners last, and understand, everyone who's listening to this, this is strictly

hypothetical. It's inconsistent with the Bankruptcy Code. I'm sorry.

MR. GORDON: I forgot about the overflow. Sorry.

THE COURT: Well, and this is being recorded. Anyway, it's inconsistent with the Bankruptcy Code. However, whatever hypothetical you create, and the governor says, you know, "We've got to comply with state law. I'm authorizing this bankruptcy, but the municipality's plan has to comply with the state law that sets forth these priorities." Is that a proper authorization or not?

MR. GORDON: I would say not.

THE COURT: Okay.

MR. GORDON: Well, it's --

THE COURT: Now you're saying that when state law says the priority has to be given to pensions --

MR. GORDON: Well, let me back up.

THE COURT: -- that's not proper if it's inconsistent with the Bankruptcy Code.

MR. GORDON: Actually, I would say -- no. I would say that the authorization is proper, but, again, a portion of that authorization is actually going to come into conflict with the Bankruptcy Code itself, so I think it's just a flawed concept. So if you had that provision in there, I -- you know what? The difference is -- let me think about this. I think the difference is the cases such as Vallejo and

others dealt with situations where someone tried to cherry pick various provisions of the Bankruptcy Code after they got into bankruptcy. It didn't involve the actual state authorization. So here I think if you were presented with that, you would have two choices. You would either have to acknowledge that state authorization as is and agree to that structure and say that will supersede the Bankruptcy Code because that's the only way the state is allowing you to get into bankruptcy, or you would have to dismiss the case.

THE COURT: Which should I do?

MR. GORDON: In that situation, I think you would give the state the opportunity to decide, but in the first instance, if the state doesn't do anything, you would have to dismiss that case because you don't have the authority to amend the Bankruptcy Code.

THE COURT: I would have to give them the opportunity to revise the authorization?

MR. GORDON: That's correct, your Honor. They'd either have to amend the --

THE COURT: How could --

MR. GORDON: -- authorization or understand that if they go into --

THE COURT: How could the governor provide an authorization that's inconsistent with the state statute?

MR. GORDON: He couldn't. He would either have to

go back and --

THE COURT: What's there to revise?

MR. GORDON: -- change the statute -- he'd either -- he has two choices.

THE COURT: Oh, go back and change the statute.

MR. GORDON: There are two choices. Either the Court agrees to allow the case to go forward with that structure because that's the only way the state will authorize it and that's what 109(c)(2) talks about, or if this Court for some reason believes that that is in conflict with the Bankruptcy Code, then this -- I guess I don't know. The state could either -- the state would have to go back and amend its statute in some fashion. I don't really know, but I think that if the state --

THE COURT: Or if it's constitutional, amend its Constitution?

MR. GORDON: Wait. What couldn't be done is that this Court could not accept the authorization and then say, "I'm cherry picking. I'm not allowing that part of the state statute to stand because that is the only way that they got into bankruptcy in the first place." That's my answer, your Honor. All right. Can I move on?

THE COURT: You can.

MR. GORDON: We're really out of time here probably, I notice, in a minute, but I just wanted to touch upon

collateral estoppel because I promised I would unless your Honor has a different --

THE COURT: No, no. You argue what you like.

MR. GORDON: As far as collateral estoppel is concerned, your Honor, the city and the state have argued that there was not a full fair opportunity to litigate in the Webster matter. We've addressed that in our papers. We believe that that is not accurate. There was full briefing. Both sides filed cross-motions for summary disposition, so they addressed the merits of the matter. The Court acknowledged that there had been briefing and oral argument before it entered its order. The city and the state also argued that there was no privity between the city and the defendants in Webster, but on September 19th, your Honor, the city argued in this court that there was a common interest agreement between the city and the state and that there was common interest with respect to the financial situation of the city and the bankruptcy, so privity is certainly there. And then finally the city and the state argued that the state court doesn't have authority or jurisdiction to rule on eligibility issues. The Webster court didn't rule on eligibility issues. It doesn't mention 109(c)(2) of the Bankruptcy Code. It merely ruled on the interplay between two state statutes, PA 436 and the pensions clause, and ruled that those two had to be harmonized and that, therefore, any

authorization of a bankruptcy under PA 436 must comport with the pensions clause or otherwise it was unconstitutional, so it did not infringe on this Court's jurisdiction in that regard. So we think that collateral estoppel is valid and applies here under the Webster judgment.

THE COURT: Thank you.

MR. GORDON: Thank you, your Honor.

MS. CECCOTTI: Good afternoon, your Honor. Babette Ceccotti for the UAW.

THE COURT: Good afternoon.

MS. CECCOTTI: And with admittedly some trepidation, I am also going to cover the authorization under state law, and I think -- I guess I'd like to start with just a couple of threshold comments. First, I think the exchange that you've had with Mr. Gordon and perhaps with others -- and I'm sure it's not going to be limited there -- will probably lead you to conclude that at least some of the issues that you've slated as purely legal will -- are better served awaiting the outcome of the trial. I'm just -- you know, Mr. Gordon took you through a series of numbers. There are all kinds of facts and information that are probably best developed through the evidentiary record, and that may well inform your Honor's views of a number of the questions that you've asked here today so far, so I'll just start with that observation. I'd like to just, if I might, also --

THE COURT: Well, just so the record is clear -- and I may have indicated this before even perhaps in writing -- it's certainly not the Court's intention to rule on these issues before the trial, and to the extent any of the facts that come out at trial bear on these, sure, they'll be taken into account.

MS. CECCOTTI: Thank you, your Honor.

THE COURT: But I did hold out to all of you that one of the purposes of today's hearing was to see whether there are any genuine issues of material fact in advance of the trial so that you can address those at the trial, and I intend to do that.

MS. CECCOTTI: Thank you, your Honor. I guess the -- let me just interject another thought into the exchange that you had with Mr. Gordon on your hypothetical, a couple of thoughts. First, the -- and I will -- I'm going to start and go through this in a little more organized way, but I just wanted to make sure I get this point out. It's important to keep in mind that as inviolable and as absolute and as definitive as those of us on the objectors' side believe the pension clause is and as much as we believe that it was the right of the citizens of the Michigan -- of Michigan to so provide in adopting it, remember that we are here in the public sector. We are not in the private sector where there is a federally regulated and federally

established pension insurance system so that when plans get underfunded, when plan sponsors are overburdened, there is a system that takes over. And I would have to say all -- certainly the lion's share of the decisions that have come down on this topic arise because of the -- because of the way that that system is constructed. There's a federal agency that provides a safety net. You know, there are moral hazard issues. There's a whole balancing that goes on in that system. We don't have that here. Michigan pensioners have Article IX, Section 24. That's it. That's what they have. So as, you know, perhaps a -- it might take a bit of a leap to see that that section means what it says and really, really, really means what it says, I think it's important to bear in mind that that is a safety net for pensions for Michigan pensioners. Okay.

So, now, to try to get back a little bit towards more of an organized progression here on the 109(c)(2) issues, the governor, as we've been discussing, had issued the letter of authorization -- the letter of authorization without any contingencies, so I think it's in -- and your Honor asked the question this morning -- a couple of questions this morning that have to do with, you know, where's the impairment and where's the harm and questions of that nature, and why wasn't the governor's reference to 943 sufficient. So I think what's important to do first is take

a look at -- briefly just take a look at the authorization letters. And, again, this is without reference to any testimony or anything else that you're going to hear next week. You know, just looking at the letters that were attached to Mr. Orr's declaration, the July 16th authorization makes quite plain in his situational overview -- he says for an extended period of time, the city has simply failed to make the investments required to provide its residents with an adequate quality of life as limited resources have been diverted elsewhere. He says the city's urgent need to address large and growing legacy liabilities and other substantial debts is self-evident. Failure to address these liabilities will prevent -- excuse me -- prevent the city from devoting sufficient resources to providing basic and essential services to its residents. Indeed, significant additional resources are required to improve health and safety. And he goes on to say that the city must devote a larger share of its revenues to effectively providing basic essential services to current residents, attract new residents and businesses to foster growth and redevelopment, ultimately begin -- and ultimately begin what will be a long process of rehabilitation and revitalization for the city. The city's debt and legacy liabilities must be significantly reduced to permit this reinvestment. Plain as day in Mr. Orr's letter. He

incorporates his entire proposal, the -- I don't have the whole thing here. I've just got some of it. This is the June 14th proposal. Goes to the governor, and the governor writes back again providing the authorization and saying in part that he's reaffirming his confidence that Mr. Orr has the right priorities when it comes to the City of Detroit. I am reassured to see his prioritization of the needs of citizens to have improved services. I know we share a concern for the public's -- for the public employees who gave years of service to the city and now fear for their financial future in retirement, and I'm confident that all of the city's creditors will be treated fairly in this process. We all believe that the city's future must allow it to make the investment it needs in talent and infrastructure all while making only promises it can keep. So I think it's very clear from these letters -- excuse me -- as it is abundantly clear from the proposal that the city is proposing to take resources from what it's calling the legacy liabilities or, fill in the blank, accrued pensions, and divert those resources to the list that Mr. Orr has laid out here, reinvestment and services and the like, so when we talk about not impairing the pensions and who took what action and when does the impairment happen, the governor's letter, we submit, in fact, is the impairment because it has -- the governor is stating that he is acknowledging Mr. Orr's priorities,

including the priorities to take money from the pensions and use them to pay other things. And so when the pension clause talks about -- excuse me. I'm sorry. I just lost my brief. I apologize, your Honor. I think I -- I have it. So when we talk about the text of Article IX, Section 24, "The accrued financial benefits of each pension plan and retirement system of the state and its political subdivisions shall be a contractual obligation thereof which shall not be diminished or impaired thereby," and we look and we are -- we see that among the records in the constitutional convention is the explanation that Article IX, Section 24, quote, "requires that accrued financial benefits of each pension plan and retirement system of the state and its political subdivisions be a contractual obligation which cannot be diminished or impaired by the actions of its officials or governing body," the impairment occurs when the governor signs this authorization with no contingencies. That's when it happens. So not impairing thereby, meaning -- means very specifically this document, and the "this" I'm holding up here now is the governor's consent. Now, why is --

THE COURT: Oh, but this raises two questions.

MS. CECCOTTI: Sure.

THE COURT: Is there a scenario in which the city would have the ability to meet its pension obligations in the very long term unless it makes the kind of investments that

Mr. Orr and Mr. Snyder have suggested should be part of the city's priorities? That's question number one. Question number two is actually a much more important question, and that is is question number one a question for now, or is it a question for plan confirmation?

MS. CECCOTTI: It is absolutely a question for now because --

THE COURT: What's the answer then? How can the city maximize its chance of paying its pension obligations unless it makes the kind of investments that Mr. Orr and Mr. Snyder are talking about?

MS. CECCOTTI: It may be that the investments themselves or the idea for the investments is fine. The question is can it get there lawfully by taking money from pensioners? That is the question that the state Constitution answers by saying no. Now, as Mr. Gordon pointed out or as I think is evident from his presentation, there's a lot of numbers here, Judge. There were numbers in Mr. Orr's request, his July 16th request. You're going to hear an awful lot about those numbers and what they are and what they are not, so I would suggest that the notion that we somehow have already today, quote, no reasonable alternative in the words of PA 436 I would suggest very much should await your Honor's review of the evidence on all of that, so --

THE COURT: Okay.

MS. CECCOTTI: I realize it's a question that has been on your mind all day, but I really think unless you really want us up here freelancing numbers -- and you really don't -- that it is best to simply --

THE COURT: I'll grant you that one.

MS. CECCOTTI: Right; right. But I guess my point is the answer cannot be because the problem seems hard, we're just going to try to find a way to say perhaps that this language doesn't mean what it says because I think once you start down that road, you run into all kinds of problems. You run into the Chapter 9 dual sovereignty problems. You run into problems of who gets to decide what, right, whether this Court gets to construe Article IX, 24, to, in fact, say it can be invaded. These are problems that are simply too thorny -- certainly too thorny to start with, and maybe we'll see where your Honor is after the evidence.

Okay. So why isn't the reference to 943(b) enough, and I think -- and I think you've heard it, but just to say it again and hopefully crystalize it a bit, I think the governor assumed in wording the letter the way that he did that somehow this all gets sorted out, and I think that seems to be a lot of the presumption here, and I must say I am not in full company with those who say that once you cross the threshold of 109(c) using state law that somehow you can start, you know, running around employing federal supremacy.

I think that that -- we'd probably have a lot more conversations about that with a lot more time with a lot more specificity before we get there. We think -- and we spent a bunch of time on this in our brief, Judge, and given your handling of the Addison case you probably didn't need all of this, but our view is that you must look -- in order for Chapter 9 to be constitutional, you have to look at all of these pieces that import or give recognition to the state law. Just to take you back to another colloquy that you had with Mr. Gordon and why I think maybe that the Chapter 13 example isn't a good fit here, 109(c) says that an entity may be a debtor under Chapter 9 if and only if such entity is specifically authorized to be a debtor under such chapter by state law. So while we're all here today obviously under 109(c) and 109(c) is in the Bankruptcy Code and so you're right -- the law that must be applied is state law, and the Court decides whether -- you, the Court, you, the Bankruptcy Court, decide under 109(c) whether, in fact, the municipality is specifically authorized to be a debtor under Chapter 9 by state law or by a governmental officer empowered by state law. And so I think that that may help to distinguish the Sixth Circuit case that you discussed with Mr. Gordon, but it also points out that getting through the door is a state law question. 903 and 904 are obvious limitations on the Court's authority. 943 is a limitation on the plan. All of these

things work together, and I think your Honor's opinion actually in the Addison case on the motion to intervene was exactly right in recognizing the limitations not only of the Court's caution in addressing the questions precisely because of the questions that 903 -- the issues that 903 and 904 import into the bankruptcy process, but another observation which takes me back to the letters and the taking of the money from the pensioners and putting it towards something else, which is, I think, your court -- your observation in that case that Chapter 9 is about debt adjustment and should not be overburdened I think applies very well here, too, and I think, again, when we get to the trial and the full array of the plan and everything else comes out and we start talking about that in the evidentiary context, I think that it is at least a question as to whether or not this issue that we're all talking about here is in a narrow sense debt adjustment or whether it is more than debt adjustment and whether that shouldn't inform the Court's caution in ensuring that the state law is being adhered to.

And I guess -- and I don't often get to the point of imploring at the podium. It's not always pretty, but I'm going to break my rule on this whole subject of where is the impairment. To me it's like a shell game. Okay. Under which of these cups is the impairment; right? Is the impairment -- I've told you where I think the impairment is;

right? I don't think the Court impairs. The debtor proposes the plan. Under Chapter 9 only the debtor can propose the plan. The debtor was supposed to have come up with something that passes muster to meet the 109(c) criteria in advance of getting to this point, and they --

THE COURT: Well, but the proposal of a plan, the filing of a plan which proposes to impair pensions doesn't result in the reduction of anyone's pension check any more than the filing of the case did.

MS. CECCOTTI: Your Honor, I --

THE COURT: That doesn't happen until the Court confirms it under law.

MS. CECCOTTI: And, your Honor, then why are we talking about it? Why are we talking about it?

THE COURT: Answer that question.

MS. CECCOTTI: If it hadn't been --

THE COURT: I'm having my issues with that very question. Why are we talking about it?

MS. CECCOTTI: We're talking about it because it's in their proposal. We're talking about it because it was in the authorization that went to the governor. We're talking about it because the governor clearly recognized it or at least recognized it sufficiently to draft the letter that he did. We're talking about it because despite weeks and weeks and weeks, no one has disabused the pensioners of the notion

that their pension rights are -- that they are intending to impair their pension rights. That's why we're talking about it. It simply does not -- here they are in Chapter 9; right? They're in Chapter 9. They've got the benefit of the automatic stay. They've gotten their stay against the pre-petition lawsuits. They want to have a bar date motion. They're getting all of the -- you know, all of the features, right, of Chapter 9. And the threshold question that has to be asked is can they be here, and the threshold question can only relate to the form in which they show up on the court's doorstep. And the form in which they show up on the court's doorstep is the June 14th proposal, which is abundantly clear on the subject of invading -- impairing accrued pensions. What else would the Court -- what else would we be dealing with? What else would your Honor be dealing with if not for the fact that they evidenced their plan?

THE COURT: I think the answer to that question may be the governor's authorization. He says we are here to adjust the city's debts in conformity with law.

MS. CECCOTTI: He says that at that end we do that, but what does it mean -- what is supposed to go on before we get there? It can't be that we have a sort of quasi eligible debtor going through all of the -- you know, using all of the processes I just described and then we have a big conflagration at the end. I mean it just --

THE COURT: Why not?

MS. CECCOTTI: Chapter 9 presupposes through the front door under state law, specially authorized under -- by state law. That is what 109(c) says. It is plain as day. And state law means state law, and it requires giving -- if they hadn't put in this -- the pages --

THE COURT: So in response to my question to Mr. Gordon, you would say that if state law requires a different priority scheme than the Bankruptcy Code, the municipality is eligible only if the Court is willing to enforce that state law priority scheme rather than the Bankruptcy Code priority scheme?

MS. CECCOTTI: I think that I would say that if a state legislature -- we're not talking about the Constitution here. You're just talking about, in effect, the PA 436 of whatever that state is. I would say that those are the terms. We have -- we allow the states -- states have a variety of authorization. Some of them have no authorization. It is a state-by-state --

THE COURT: Every bankruptcy case that has addressed that question has held the other way, hasn't it?

MS. CECCOTTI: Well, I don't know the answer to that, your Honor. In the Chapter 9 context?

THE COURT: Yes, in the Chapter 9 context.

MS. CECCOTTI: Okay. Well, I --

THE COURT: Every Bankruptcy Court has held once you're in the door, it's the Bankruptcy Code priorities that apply, not the state law priorities --

MS. CECCOTTI: Right. Well, right. And now we're getting into the --

THE COURT: -- because the state consents to the Bankruptcy Code or it doesn't.

MS. CECCOTTI: Well, and I would say that a state that passes a law such as your Honor proposed maybe, in fact, looked at those cases and said, no, we don't really want to go there. We want to -- you know, we'll let you go if it's this other way. I think the through the door -- once we're in the door -- I know what Harrisburg says. You know, I have a lot of trouble with it just because I think that the doctrine has not evolved in a sufficiently precise manner. You don't always see what the conflict is. You have to come up with notions of what the purpose is. Remember the ancient Supreme Court cases here said bankruptcy is about discharge; right? So can states have discharge laws? So we're way, way far away from that now, so I think -- again, I think we'd have to have a lot more conversations about what happens through the door. Right now we're talking about you're at the door, and you're at the door, and you're presenting yourself, and what you're wearing, right, is something that says we are going to violate Article IX, Section 24.

Just want to see if there is anything -- see if I've left anything out here that I wanted to cover. I have some minutes here. I guess I could barter away my minutes, Judge, or I could give them to you to barter them away. Let me just take a quick moment here. I think -- I mean, again, I think we're going to get to the point of duplication if I continue unless, your Honor, you'd like to ask me anything else. I think I've hit the points I wanted to hit.

THE COURT: Okay. Thank you.

MR. WERTHEIMER: William Wertheimer, your Honor, on behalf of the Flowers plaintiffs. As I'm sure your Honor will recall, although it seems like ages ago now, the Flowers plaintiffs were plaintiffs in one of the state court cases that preceded the bankruptcy, a state court case in which we were making the claim that under state law the governor was required to recognize Article IX, Section 24, if and when he authorized a bankruptcy. I'm not here to speak on bankruptcy law. When I heard the reference to Asbury Park, I thought of the street in northwest Detroit. I'm not a bankruptcy lawyer.

THE COURT: Okay.

MR. WERTHEIMER: I just want to speak briefly on the state law, which it was my understanding at the stay proceedings everybody kind of understood, including the city attorneys, that although our claim was being delayed, it was

not being changed in terms of its nature; that is, that this Court would decide as a matter of state law whether this bankruptcy was properly authorized. It was just that the forum was changing.

And I'd just like to make three points as to that state law, three areas where I think this Court can look to what it should do in deciding what I believe is that state law issue; that is, the basic eligibility issue. If you look at the equivalent of legislative history of Article IX, Section 24 -- that is, the constitutional convention record -- there is certainly references to the fact that has been mentioned here today that it was meant in part to deal with the fact that pensions had been considered not to be a matter of contract, but the only specific reference that I found in that record -- and no one has cited anything to the contrary -- is the comment of Mr. Van Dusen, which I -- with the Court's permission, I'll take the liberty to quote. It's not long. "An employee who continues in the service of the public employer in reliance upon the benefits which the plan says he would receive would have the contractual right to receive those benefits" -- he didn't stop there -- "and" -- he didn't say "meaning" -- he said "and," in addition -- and I think this goes to what Mr. Gordon was getting at, "and would have the entire assets of the employer at his disposal from which to realize those benefits." That was the

understanding of Mr. Van Dusen. There's no contrary understanding on the record as to what the idea was on behalf of the people who were writing Article IX, Section 24. That's point number one, and I think if you look at what Emergency Manager Orr did in his June 14th proposal, Mr. Van Dusen, were he alive to take a look at it, would say, "That's not what I meant," because on June 14th what Mr. Orr proposed and he continues to propose is the retirees get treated like any other creditor. He didn't say words to the effect of "all the assets of the employer," so that's the first piece of state law in the broad sense of the term that I think you can look to.

The second piece is the Webster and the Flowers cases and the retirement case. And I'm not repeating Mr. Gordon's argument relative to collateral estoppel or the res judicata argument. I'm simply pointing out that as -- excuse me -- as Mr. Gordon indicated, that case was fully briefed, and a state court judge looked at the exact issue -- well, maybe not exact but very close to the issue that is in front of you, and that state court judge, after full briefing, decided that in a manner consistent with our position. And I would point out there is no contrary law anywhere. I recognize this Court -- the cases that say you look to the definitive ruling from the highest state court and all that, but Judge Aquilina's decision -- decisions,

well-reasoned, are all that's out there. She's a state court judge deciding this issue. That's the second piece of state court law that, as far as I can tell, is out there.

There's one other, and that is we have the state attorney general. This isn't law, but the state attorney general enters an appearance a little late in the game. The governor has already authorized the bankruptcy. However, the state attorney general, as an officer of the state, as the chief legal officer of the state, tells this Court that Article IX, Section 24, binds the emergency manager in bankruptcy. Now, we all know that that gets into the issue of is it at the eligibility stage or the plan stage, and I -- that's been dealt with. My point is simply that a state officer, the attorney general of the state, saying that the emergency manager in bankruptcy is bound by Article IX, Section 24, is consistent and supports our position that the governor, when he goes to authorize that bankruptcy, is also bound by Article IX, Section 24. And with all due respect to the governor, we think it's up to this Court to hold the governor to that.

THE COURT: All right. Thank you, sir.

MR. WERTHEIMER: Thank you.

MS. PATEK: Good afternoon, your Honor. Barbara Patek on behalf of the Detroit Police Command Officers Association, the Detroit Police Lieutenants & Sergeants

Association, the Detroit Police Officers Association, and the Detroit Fire Fighters Association defined in this case as the Detroit Public Safety Unions. As the Court is aware, these are the men and women who provide the police and fire protection that are essential to the survival of the city, and these are exactly the essential services that Chapter 9 was designed to preserve and protect.

I want to use my time this afternoon to talk a little bit about ripeness, talk very briefly about the supremacy clause and the tension between the supremacy clause and the Tenth Amendment, and then to try to answer some of the questions that the Court has raised with some of the other objectors today.

On the issue of ripeness and why this is a question for eligibility, I think that goes to the very nature of Chapter 9, which precisely because of the sovereign immunity and the sovereignty of the State of Michigan, this Court, as it's recognized in so many hearings, is limited in what it can order the city to do. In that respect, this -- not that every bankruptcy isn't a consensual process and not that every bankruptcy doesn't involve a lot of negotiating. Chapter 9 is unique because it incorporates -- it's a largely consensual process at some level precisely because this Court cannot trump the state's sovereignty in particular situations. And in that regard, if one talks about imminent

harm, there is -- you know, it's in the record. Mr. Gordon alluded to the fact that the stay authorized the city to come in this court for a very public purpose, and that purpose was to impair the accrued vested pension rights of its public servants. That question, as the city points out in its papers, no court has ever said they can't do it, and no court has ever said they can. It's an unanswered question. We're entitled to know what our rights are, and to suggest that by knowing what our rights are in the door that is to knowing what -- to know what the proper authority is here would somehow skew the process or cause people to walk away from the table I think is wrong. This is a hard question that the Court has to answer, but the Court is here to follow the law. I think this is -- there is imminent harm to these individuals here, and there's a second piece of that by virtue of the vacuum in which there's no legal precedent on this issue, and that is -- I'm just going to throw out to the Court the idea that this is one of those issues where it's capable of repetition but evading review. If every time this gets kicked down the road to confirmation, nobody is ever going to know what their rights are when this issue comes up. I submit that Michigan is a little bit unique, but I think that there are plenty of reasons that this issue is ripe for adjudication today.

I'd like to take a crack at some of the questions

that the Court raised. You raised the issue of what if the state law requires a different scheme of priorities than is authorized by the Bankruptcy Court. I think if you step out of the weeds on that question and I think you look at what the Code says here, the state has to give its consent to come into Chapter 9. And in giving its consent, the state agrees to certain provisions of Chapter 9. I think a state that authorizes such a scheme simply can't give its consent to come into Chapter 9. I think that's the simple answer to that question.

THE COURT: So your answer then in that hypo would be not eligible?

MS. PATEK: Correct. I also think -- the Court asked the question and raised the 11th Amendment, and I'm going to go out on a limb here on this and the question of sovereign immunity because I think the answer to a lot of the issues before the Court and whether or not, in fact, the city can impair these rights or use the Court to impair those rights is in some ways answered by the Code. Section 106 of the Code addresses the sections of the Code under which the state waives its sovereign immunity. 109 is not one of them, and I think that makes the eligibility issue as it's framed by 109 a question of state law. And the other place, if we're going to jump ahead to where we'll be down the road, where the state does not waive its sovereign immunity is

under Section 943. We know there are some places where to consent to come into this Court and get relief the state has to agree to conform to the rules. 365 is one of those that you've got Bildisco. If you're going to come in and you look at -- that's a place where the state has to agree, consent to be governed by the federal rules. The other place is the automatic stay. But when you get down the road to the plan that only the city can propose, the state does not waive its immunity, and that --

THE COURT: I think you might be overanalyzing my question about sovereign immunity. I was only analogizing to the 11th Amendment cases that hold that the issue of whether sovereign immunity is waived is a federal issue, not a state issue. I didn't mean to suggest, as you appear to understand here, that there is -- that there are 11th Amendment issues in this case.

MS. PATEK: I'm not suggesting that you are, your Honor, but I'm suggesting that -- and this sort of brings us back to where Ms. Levine started out this morning with this concept of -- this very basic concept, and one of the things that makes this case so hard and one of the things that all the commentators agree makes Chapter 9 so hard is this tension. We have a federalist system. There are rules of the road that were set up by the founders. We have a limited system of federal government. All the other powers are

reserved to the states and the individuals. And there's no question that wasn't done so that we could have big and powerful states. That was done by the founders so that the individuals close to the ground would have their rights preserved, and I think within the structure of Chapter 9 and within the limits of the Tenth Amendment, that the state simply cannot use Chapter 9 to impair an express constitutional promise. And I want to talk about that issue for just one moment. This pensions clause is in a very unusual place. Okay. This is -- I think it's fair to say -- you talk about there is a contracts clause in the state Constitution just like there's a free speech clause and there are a lot of things that mirror the Bill of Rights, but, as Ms. Levine told us this morning, if somebody is violating my free speech rights, I'm not in state Circuit Court. I'm looking to the federal courts and the federal government to protect those rights. If you're talking about fiscal management, then that's a state issue, and in this case this state and the people of this state chose to enshrine that right to vested accrued -- this isn't all pension benefits, this isn't future benefits, just what people have already earned -- in its state Constitution and say those cannot be impaired.

The Court asked the question about what if there's not enough money, which sort of brings me back to the first

issue I was talking about. This Court has to rule on the legal issue that's before it, and if there's not enough money just like if you're in a Chapter 11 that you don't want to see liquidation, that's a hard question that the creditors, including the pensioners, including my clients, have to answer along with the city and try to solve this problem within the limits of Chapter 9 because if we don't solve the problem, the only remedy is a dismissal.

THE COURT: Well, I guess even that answer troubles me because if the Court holds here that there is this pension right that cannot be impaired and because the governor didn't condition this filing on the city recognizing that right in the bankruptcy, what would happen upon dismissal? There'd be this court holding that there's this unconditional absolute right not to have pensions impaired. On behalf of your retirees, you couldn't negotiate that, could you? How could you?

MS. PATEK: I can't negotiate that upon my retirees, but I suggest to the Court there is a solution to this problem, and the solution is for the city to come back again and to authorize -- have the state authorize the filing within the confines of the Constitution, and we move forward on that basis. I don't -- I understand that this has -- you know, we talk about the elephant in the room, but the larger part, the healthcare benefits, are not protected, and the

city has already said effective yesterday -- and these aren't my clients, but -- we're done providing that. It's a significant claim. I don't want to minimize that, but I think it is something, given our constitutional structure, that has to be dealt with in the confines of these proceedings, and there are negotiations. There's a huge consensual component to this, and that doesn't stop if the Court rules the way that we've asked to rule.

I see my time is up. I just want to wrap up very quickly, and I guess I would say we came into court on the first day, and we supported the city, and we've supported the city in many respects throughout this. We agree that there should be the stay. There has been the breathing space. But I think this is a hard, difficult question. As Ms. Levine said, democracy is hard. This restructuring plan has to be devised in accordance with applicable law, and the city on the front end has to agree that it's going to -- it's going to do so, and in the absence of that, I think they're not eligible. Thank you, your Honor.

THE COURT: All right. Thanks to each of you. We'll take our afternoon break now and reconvene at 3:20, a half an hour from now, for the city's arguments.

THE CLERK: All rise. Court is in recess.

(Recess at 2:50 p.m., until 3:20 p.m.)

THE CLERK: Court is in session. Please be seated.

Recalling Case Number 13-53846, City of Detroit, Michigan.

THE COURT: And it looks like everyone is here.

MR. BENNETT: Good afternoon, your Honor.

THE COURT: Mr. Bennett, you may proceed.

MR. BENNETT: Good afternoon, your Honor. Bruce Bennett of Jones Day on behalf of the city.

THE COURT: The only thing I would ask of you, sir, is to leave enough time before our closing time today for me to ask some questions of Mr. Todd. Doesn't need to be now. It can be whenever it's convenient for all of you.

MR. BENNETT: Okay.

MR. TROY: Mr. Troy, your Honor.

THE COURT: Mr. Troy. I'm so sorry, sir. And so I want to do that today because I'm not sure what his travel plans are.

MR. BENNETT: Okay. Your Honor should feel free to interrupt me if you think I'm getting too close to the end. And I actually have one procedural question that I'd like to get settled, too, which really has to do with whether you're expecting or would benefit from oral argument at the beginning of the next -- opening argument at the beginning of the next phase because that's -- so I don't know if --

THE COURT: You mean tomorrow?

MR. BENNETT: No. On the evidentiary phase beginning next week.

THE COURT: Oh, well not so much oral arguments as opening statements.

MR. BENNETT: Opening statements is what I mean.

THE COURT: Yes.

MR. BENNETT: Okay. Great.

THE COURT: Yes. I think opening statements are very important.

MR. BENNETT: Okay. I want to start with some general comments, some of which are designed to respond to things that came up this morning and some of which I think just help, I think, set the stage for what at least the city believes is happening in this Chapter 9 case. And I want to start by saying that the purpose of the Chapter 9 case is to adjust the city's debts, and that means all of their debts, obligations evidenced by bonds, obligations under other contracts, obligations to provide healthcare, and pension obligations. And so that there isn't any confusion, there's been a lot of reference to statements that were made. I think the statement most cited and the one that I think is -- it's the same as all the other ones that have been made -- is that there must be -- the statement was there must be significant cuts in accrued vested benefits. It's been cited often, and it's true.

I want to make a couple of clarifications. I don't think anyone for the city ever said we were going to

eliminate pensions. This has been about the underfunding amounts. It is the underfunding amounts that are problems. I think your Honor understands that, but I think it's important to remind everybody else that we've never said that the objective is to eliminate pensions. The objective is to address the underfunding situation.

Now, why did we make that statement? The statement --

THE COURT: Well, let me just put it right to you. Is it your intent to propose a plan to reduce pensioners' monthly checks?

MR. BENNETT: To be very technical about it, what we have -- what we have -- what we have noted is that it is impossible for the city to fill the underfunding gap in the existing pension trusts, and we have also said that likely requires changing the amounts of pension benefits. Now --

THE COURT: By "changing," you mean reducing?

MR. BENNETT: Reducing. Now, I do want to -- I'm going to skip a couple points and then come back. Notwithstanding the fact that the Chapter 11 case has been filed, it remains the city's hope that these adjustments will be achieved on a consensual basis pursuant to agreements reached with the holders of the obligations. That is still the objective. And, of course, we are participating in mediation that's intended to facilitate that goal, and,

frankly, we'll meet with anyone anyplace anytime to try to achieve that goal. And we're going to discuss at certain points certain statements that have been made by others in this case about this problem which may suggest that those discussions are going to be particularly difficult, but I want there to be absolutely no confusion about where the city -- where the city stands on this.

And by the way, the filing doesn't say how ultimately this case is going to end, whether it's going to -- whether we're going to have a consensual plan, whether we're going to have a nonconsensual plan, whether it'll be partly a consensual plan or partly a nonconsensual plan. And although the city did make a proposal that certainly contemplated cuts to the underfunding obligation and ultimately to benefits that absolutely is a part of the June 14th proposal, it was a proposal in an out-of-court negotiation, and I want to submit -- and we're going to come back to this point later -- it can't possibly be impermissible to ask to reduce benefits, particularly when you can demonstrate a need to do so. And so far, frankly, that's what the city did pre-petition, and so far that's what the city has done post-petition. We haven't filed a plan yet. It will come soon. And there has not been a request for cramdown, so -- and I think as we get into other parts of the argument -- the fact that we don't quite know what's

coming later may have some bearing on some of the legal points that your Honor has talked about and that others have talked about earlier today.

THE COURT: Is it the city's position that the State of Michigan does not have the obligation under the Michigan Constitution to guarantee the city's underfunding?

MR. BENNETT: I don't know if the city has a position. I will tell you that I have read all of the materials probably more than anyone else in the city's team, and I don't think the state has an obligation to guarantee the pension obligations of a municipality. I think actually when you look at the --

THE COURT: Isn't it in the city's best interest to say that -- or to assert that the state does have that obligation?

MR. BENNETT: I don't know whether it is or is not in the city's best interest to even take a position on that point, and that's why I said I don't think the city has a position on that point, but I have done a lot of the work, and I think I've made up my own mind as to what I think is there. I do think it's in the city's position that if we could get money from the state, we would want it, and it would be a great thing, and I'm reasonably certain that that sentiment has been expressed on more than one occasion.

THE COURT: Well, is there any reasonable prospect

that the state will comply with that request in the absence of a legal obligation -- a determined legal obligation?

MR. BENNETT: I don't know the answer to that question. Thus far the state has been of the view that the city has to reorganize based upon its own financial resources.

Okay. The next point I wanted to touch on is the fact that there are a large array of state and federal statutes that say in all kinds of different ways that the city is obligated to pay its debts. In fact, they say that the city is obligated to pay its debts in all kinds of different ways. And the city itself and the state has no -- and we'll get into this in much more detail -- no ability in order to overcome those laws or very, very, very limited ability to overcome those laws. One important point about them that didn't --

THE COURT: You mean comply with those laws?

MR. BENNETT: No. To overcome them to get past them if they can't pay all of their obligations. And, again, it's a situation that the city is going to prove it's in, but that's for another hearing. The point I wanted to make here that I don't think was made earlier today was that a lot of these priorities collide with each other in all kinds of different ways. We heard, by the way, about the all assets at their disposal comment that was, I guess, from the

constitutional convention. Assuming for a second that that is what was intended, the problem is is that the legislature has also passed a law that describes certain debts -- the obligation to pay certain debts as a, quote, "first budget item," close quote. I don't remember the rest of the sentence, but those words are there. There's also other state statutes that don't actually grant a lien but that say proceeds of certain things must be used in certain orders to pay. And when you sit down and try to figure out in any environment where you don't have enough, how do you fit all these different things together, you run into a problem very, very, very quickly. And these are the provisions, by the way, that are protected by the federal contracts clause and also by the Michigan contracts clause because many of these provisions are in ordinances or resolutions that form part of bond contracts, and others are in ordinances and resolutions that form part of employment contracts. So you wind up -- if you look at the world before you even start talking about bankruptcy, you don't just have coherent commands, this is how you pay and this is how you go about doing it and everything works, you have a whole bunch of priorities that actually don't work, and this, frankly, is --

THE COURT: Well, but the objecting parties say all of those contract obligations that have protection merely under the contracts clause, federal or state, can be adjusted

consistent with state and federal law, but the pension obligation under the state Constitution is inviolate.

MR. BENNETT: And we'll get to that if you'll give me a chance. I will explain why --

THE COURT: Okay.

MR. BENNETT: -- they are, in fact, no different, but I guess my point here is that outside of bankruptcy, you have a -- you don't have coherence, and this is really to the whole point of does it really make any sense to have a rule that says if the state conditions its filing a proceeding based upon complying with its priorities, what do you even have. And in many circumstances, you have something that is just not meaningful in the context of where there's not enough to go around. I think that's the narrow point for the time being. We will generalize when we get to the whole issue of how the --

THE COURT: Okay.

MR. BENNETT: -- different clauses work. I also want to say that contrary to the papers that were filed -- and I'm now referring to the UAW's papers -- the June 14th proposal didn't take broad aim at the city's workers and retirees. It was very, very carefully drafted to try to treat as many classes of creditors the same as we possibly could denying preferences to any except in cases where we were legally compelled to provide them. We thought and the

emergency manager thought that that was the best way to go about the problem that confronted us, and, of course, we're not under any illusion that that's going to be the last word on this question. There will be negotiations. There will be a plan filed, which I'm certain will differ from the proposal that was issued on June 14th in part to respond to creditor input, and it will be subjected to enormous and exacting procedures by this Court before it is ever confirmed.

I also want to spend just a second about the point that was made using some of the letters, the letters that were exchanged between the emergency manager and the governor. If your Honor hasn't already, I commend you to read all of them, not just the parts that were quoted. I think it's -- I think to fairly summarize the points made in both letters, the city has been -- the city services, city residents, the ability of the City of Detroit to be a city that provides adequate services to its residents has gradually been lost as a result of the constant and consistent diversion of current tax revenue paid by current tax revenue to legacy liabilities, including but not limited to pension claims. That is the problem. It is not as if everything is fine, let's take some money from pensioners and put it to the benefit of residents to make things better. The diversion already occurred. State law has been followed. Pensions have not been impaired or diminished. A consequence

has been that the resources available for services, that the resources available for investment have, in fact, been significantly impaired and significantly diminished to the point that lots of the city's infrastructure is no longer serviceable, thus the reference to need for investment. It's not for the new and wonderful. It's to put back things that really need to be updated and, in fact, replaced because they're worn out, and it's to restore budgetary items, budgets that have, in fact, been cut too great. And I think that sense -- if you read the entire document, you will see that that is the historical view of the current situation. Again, it will be proved next week. And the solution is in part a reinvestment program. Again, just to be technically correct, it's 1.25 billion over ten years, not over five years. Five years would be better. I don't think anyone thinks we can afford it.

I think the next point and the last point I'm going to make by way of introduction is really to address one of your Honor's questions, which is what happens if the city can't adjust its debts. I think we have to start with the following. Most business owners and residents are smart enough and sophisticated enough to figure out that it's a problem to be the highest -- residents of the highest taxed jurisdiction in the State of Michigan where somewhere between 42 and 65 cents of every dollar is spent on something other

than services to current residents. That is not a stable situation. That is just not going to work out well. The consequence will be continuing declines in revenue. It may be that debts of all kinds would be paid for awhile, but ultimately debts of all kinds will not be paid, and no provision of any Constitution will change this. Thus, the stakes are very high not just for the city but also for its residents and its creditors, and I think that puts a very sharp point on your Honor's question about what is a constitutional provision worth when you're confronting an economic crisis such as this.

Unless your Honor wants to hear much about it, I was next going to talk about your jurisdiction to decide the eligibility question, but no one else raised it on oral argument, and since it wasn't raised on oral argument, I'll leave it to the papers unless your Honor has any particular questions with respect to that point.

THE COURT: No.

MR. BENNETT: And I'd like to take the same prerogative that if I intentionally pass over a topic because it wasn't covered today, if it's in our papers, we still care about it.

THE COURT: Of course.

MR. BENNETT: I'm just going to try to use time wisely. So the first place I'm going to spend some time is

on the constitutionality of Chapter 9, and I'm going to do it a little bit differently because I think, frankly, if we do a really careful look at Bekins -- and I'm going to call it Bekins because it's a really big company in California that has -- the name is spelled B-e-k-i-n-s, and everybody calls it Bekins, but I don't know what the correct pronunciation in this particular case is concerned. A very careful analysis of Bekins -- and believe it or not, the Cardozo dissent in Ashton is going to provide us with the guidepost to answer a lot of the questions that may not be constitutional questions but that ultimately are resolved by those cases. First, I have to say because it's important that it isn't this Court's place to overrule Bekins. Bekins has been the law for lots of years. And as the U.S. Attorney pointed out, it's not only that Bekins hasn't been overruled, it's actually never been challenged or questioned or otherwise suggested to be worthy of reconsideration by anything that the Supreme Court has done. And, moreover, in all of the discussion that your Honor heard about why Bekins should not be regarded as good law anymore, no one actually said that the -- that Chapter 9 has been changed in any material way from the law that was before the Court in Bekins, and that's because in all the ways that mattered it really hasn't changed, not just -- not by a little but really not at all. However, we don't want the Court to write an opinion that says, well, you feel

constrained not to overrule Bekins. You think it should be overruled. So I'm going to spend some time talking about why Bekins is absolutely right and why Asbury Park and anything else didn't change anything.

Let me start with just a quick word on Asbury Park. Even to the Supreme Court, if you read their own words, Asbury Park is kind of considered an outlier. It has -- the Supreme Court has never since approved a municipality's modification of its own contract on the basis of emergency or anything else. Every time it's been asked to, it's basically talked about Asbury as being, number one, confined to its facts and extraordinary situation and not reflective of a broad doctrine. This same argument was made to Judge Bennett in the Jefferson County case, and he commented on it. I think we've cited to that case in our papers. He does an even better job than I just did of explaining why Asbury is an outlier. It doesn't provide much comfort to any municipality thinking it's going to modify its debts without the help of the Bankruptcy Code and is no good reason to reconsider Bekins.

Now, the next thing I want to talk about is what Bekins really does, and the -- a reality that you can find in Bekins if you're looking really hard, but unfortunately you have to look really hard, is that there were two constitutional provisions at stake when the Chapter 9's

predecessor was subject to Supreme Court review. One was the Tenth Amendment, and some people have talked about that. And the second part was the contracts clause. And when you read Bekins, the Court kind of touches on all the different features that matter but isn't particularly careful about matching up which features were needed to overcome which constitutional problem. And, frankly, in there we're going to find the answers to a lot of the -- a lot of the other questions that come up in this case.

So let's start with the Tenth Amendment. Of course, the Tenth Amendment, if you quote the whole thing -- and when your Honor confronted earlier, I'm not sure the first six or so words were quoted, "powers not delegated to the United States by the Constitution, nor prohibited by it to the states are reserved to the states respectively, or to the people." For starting purposes, "powers not delegated to the United States" are important words, and one of the things Bekins very clearly says is uniform laws on the subject of bankruptcies are delegated to the United States and that laws on the subject of bankruptcies include municipal debt, and I think they used "composition" as opposed to "adjustment," but composition statutes. So it's actually not a close call that the -- at least as far as the Supreme Court is concerned -- and I think that's all that matters for this purpose is that we're going to have a municipal Bankruptcy Code that at least

covers subjects of bankruptcy and that those are clearly federal functions. Where a Bankruptcy Code applicable to municipalities --

THE COURT: Well, but we know from several Supreme Court cases that the mere fact that Congress legislates within its authority does not necessarily by itself mean that it's consistent with the Tenth Amendment.

MR. BENNETT: Well, actually I think --

THE COURT: Right? You've got Printz --

MR. BENNETT: Well --

THE COURT: -- in New York at a minimum that hold that.

MR. BENNETT: Well, that was the commandeering point. We'll get to commandeering. There's no commandeering in the Bankruptcy Code.

THE COURT: Well, I don't mean to suggest that there is, but in the laws that Congress passed that the Supreme Court held unconstitutional there, they were legislating within their commerce clause or other enumerated power.

MR. BENNETT: Okay. In the radioactive waste case, the New York case, it was because they used means that were inappropriate that offended the solvency -- excuse me -- offended the sovereignty of the states. In the Bankruptcy Code -- in the context of the Bekins case, I think when you read the case, they were worried about something different.

They were worried about the -- in Ashton the majority was clearly worried about the bankruptcy parts going too far and intruding on insolvent -- on sovereignty issues that weren't actually close enough to the core bankruptcy problem. That's where we got the governmental and political powers type exception that we have today, and so -- but I don't think there is -- your Honor is correct. If the way that the -- that Congress chose to legislate on the subject of bankruptcies affecting municipalities was to tell state courts what state courts had to do, then you would conceivably have a problem, but there's nothing about the Bankruptcy Court that tells -- state any things what states have to do. What the Bankruptcy Code tells courts, what it tells federal courts what they should do when confronted with a municipality that petitions for relief and petitions for relief with proper authorization. And so I don't think that is -- that doesn't implicate the second half of the Tenth Amendment. It only implicates the first half of the Tenth Amendment, and, quite frankly, it's protected by it.

And this is going to come up with something later. When we think about the issue of priorities -- and that's a word that encompasses lots of different things, and we can break it down further if we need to -- priorities are at the core of the subject of bankruptcy, absolutely solidly in the core, so a point I want to make and we'll come back to is

that we're not really dealing with the part of the Bankruptcy Code that gets closest to offending sovereignty. We are really dealing with -- when we talk about where pension claims stand in the world and where they can be impaired, we are dealing something that is core to the subject of bankruptcies. It's not at the edge of the things that made the difference between the constitutionality and nonconstitutionality of the Bankruptcy Code under the Tenth Amendment.

THE COURT: Well, I think possibly your colleagues on the other side might take issue with that because they analogize the pension right to a property right, which is a matter of state law, at least under our present Bankruptcy Code. It probably doesn't need to be, as a matter of constitutional law, but it is.

MR. BENNETT: We will come later, and believe it or not, it's going to be implicated in other aspects of the Chapter 9 case not having anything to do with pensions to where the line is between a priority and a property right. When we talk later -- I'll get to it later. I have a whole section on why in this instance a pension is an unsecured claim and not a property right.

THE COURT: Okay.

MR. BENNETT: If we -- just to take a short part about it now, as I read the cases, there are some cases that

talk about an entitlement to money being a property right, but in every single one of those cases the money was there, so, for example, it was in a bank account and the balance was there. In another circumstance, you were dealing with a -- an entity was reducing the amount of money that was supposed to be paid to an employee, but there was a hundred cent dollars there, and the three percent that was going to be carved out was going someplace else. There is no constitutional case that deals with a promise that there -- a promise that might or might not be satisfied because there's not enough money and say that kind of a promise is a property right. So I think that if you -- if we apply carefully the Supreme Court cases -- and when I get to them, I'll remember the citations -- we are going to find that an unsecured promise where the actual sum of money can't be pointed to because it's not there yet, that's not a property right and never has been, and so the Fifth Amendment is not implicated here. This is absolutely a contracts clause case, and we'll get to the contracts clause -- clauses in a second.

Okay. So I want to -- last point with respect to the Tenth Amendment, of course, Bekins says it's constitutional under the Tenth Amendment. The Bankruptcy Code, in particular, its part relating to municipalities, it's constitutional under the Tenth Amendment. It finds that the combination -- that apart from the fact that it's subject

to bankruptcies, it finds that the fact that the Code, then the Act, had carefully carved out governmental and political powers, kind of the -- that is, the relationship between a municipality and its subjects -- it's carved that out. It says that is an appropriate safeguard to states retaining sovereignty, and they say, "And, oh, by the way, there's a consent requirement." So those two things, the consent requirement, the -- what I'll call the 903-904 carveout, and the fact that the uniform laws on the subject of bankruptcies are fair game for the federal government, those three things are the three points that the Bekins court says it's okay for Tenth Amendment purposes.

Now, it's time to work about -- talk about the contracts clause problem. Your Honor is clearly familiar with what the contracts clause problem is. You have a contracts clause -- and I have a cheat sheet for everyone. I've provided my colleagues on my left with a copy during the break. If your Honor --

THE COURT: Sure.

MR. BENNETT: -- will, I'd like to pass up --

THE COURT: If you'd like me to look at it, sure.

MR. BENNETT: -- copies. And here we have the three clauses that we need to talk about, the federal contracts clause, the state contracts clause, and the pensions clause. As far as the Bekins court is concerned, it's talking only

about the federal contracts clause, and where I'm going is it's not going to make any difference. And what the Bekins -- the Bekins court doesn't think that consent of the state has anything to do with getting beyond this clause probably because it knows that there's no consent out to the contracts clause. Instead, it finds that the reason why that the municipal bankruptcy act is constitutional is because the entity that is actually impairing or changing contracts is not the state. It's not the municipality acting by the state. It is the court itself. And the key quote is the state invites the intervention of the federal, my word, bankruptcy power to save its agency -- that's really a synonym for municipality -- which the state itself is powerless to rescue. And the reason the state is powerless to rescue it is because of the contracts clause. Through its cooperation with the national government, the needed relief is given. So under -- so as far as Bekins is concerned, under Chapter 9 the federal government, through its courts, is the pertinent actor.

Now, you could write this more elegantly, and it wasn't in our briefs because I actually didn't find it until last night, and that is Ashton. You know, I have to confess --

THE COURT: That is what, sir?

MR. BENNETT: Pardon?

THE COURT: What did you say it was?

MR. BENNETT: Ashton. Until yesterday I'd never read Ashton. After all, everybody knew it had been overruled by Bekins. But I read it last night, and I got to the end, and I realized there was a dissent by Cardozo. And I read it because it was by Cardozo because he writes really well. And he took this particular issue head on, and so I'm going to read a lot of sentences from it. It's on page 142. And here's what he says. He, of course, is dissenting, so he's finding the last version constitutional, and he gets to the contract clause problem. And by the way, one of the things about Cardozo's dissent is that he's also much better about dividing the Tenth Amendment analysis from the contracts clause analysis. He kind of does it explicitly separately. And he says this. This is about the contracts clause. "The act does not authorize the states to impair through their own laws the obligation of existing contracts. Any interference by the states is remote and indirect." I'm going to skip some things, some citations and some things that aren't that important, and get to something that's more important. "If contracts are impaired, the tie is cut or loosened through the action of the court of bankruptcy approving a plan of composition under the authority of federal law. There, and not beyond in an ascending train of antecedents" -- it's an amazing sentence -- "is the cause of the impairment to which

the law will have regard," skipping some citations. "Impairment by the central government through laws concerning bankruptcies is not forbidden by the Constitution. Impairment is not forbidden unless effected by the states themselves. No change in obligation results from the filing of a petition by one seeking a discharge, whether a public or a private corporation invokes the jurisdiction." We're going to use that sentence again when we talk about whether -- how much we have to decide today. "The court, not the petitioner, is the efficient cause of the release."

For some reason Cardozo didn't participate in Bekins. The Bekins court, I think, said the same thing. I just think they said it a lot less clearly and a lot less elegantly.

So I think this is very informative about the right way to think about who is doing what and will become important when we get to the authorization problem, which we're going to be at very soon, but I want to --

THE COURT: Where do you think in Bekins the majority of the court or the court itself said the same thing?

MR. BENNETT: The words I read at the -- I'm sorry. I got to find the back pages. The words I started with, the -- it's at page 54. The state invites the intervention of the federal bankruptcy power to save its agency -- means

municipality -- which the state itself is powerless to rescue -- that's the reference to the contracts clause. Through its cooperation with the national government, the needed relief is given. I think the -- I think they're doing exactly the same thing and just managed to do it in a lot fewer words but with -- losing a teeny bit of precision in the process, but it is the same thing. They are basically adopting the Cardozo view of why the bankruptcy law is constitutional under the contracts clause, the federal contracts clause.

And, you know, I quoted these words, but there are words before it and words after it that basically zeroes in on that they're dealing with this particular issue at this particular point in time. This is just as much as they say.

The Bekins court, of course, there's no dissenting opinions. There's two judges that say they dissent for the reasons expressed by the majority in Ashton. That's all they do. And so that may well be one of the reasons why the court was a little bit less careful. Of course, what Cardozo said isn't precedent. It's just very, very clear thinking, elegantly written about exactly the problem we have in this courtroom today, and I think it's awfully persuasive, and I think it is reflective, although certainly done better, than the work that was done by the Bekins court.

A couple of other constitutional issues before we

move on to the authority points and the different contracts clauses. AFSCME does take the position in their papers that the contracts clause continues to constrain all municipal bankruptcies. Of course, the federal contracts clause we know from the Supreme Court does not. We'll talk about whether there's any difference in the state courts soon. But why AFSCME takes that position is they know full well that if the contracts clause is easily bypassed by a municipal bankruptcy case -- and we think that it is for precisely the reasoning of Judge -- Justice Cardozo -- then this is over because the contracts clauses, as we're about to get to, are very, very similar. They're almost identical to each other, and they're identical in all the ways that matter. We will go through it very carefully.

There was next the point that was made about accountability. I don't think there's any confusion about accountability. I think, again, I appeal to Cardozo's language but also to Bekins on this point. If you don't like the powers that a court has in Chapter 9, write your Congressman. If you don't like the way Detroit was managed so that it wound up in Chapter 9, don't let the people who used to be in office be in office again in Detroit. If you don't like the emergency manager and don't think he was qualified and don't like what he was doing, write the governor or your state legislator. There is no

accountability question if you break it down in the way that Cardozo broke it down. And by the way, the other thing Cardozo says and I think also Bekins says, there's nothing wrong with asking. You have to ask if you're going to do this consensually. The emergency manager on behalf of the city had to ask the retirement funds directly, retirees more indirectly, to reduce or change benefits in order to accommodate the needs of current city residents and the ability of the city to survive. They could also ask the Court to exercise its authority to help, too. That doesn't mean they are the one loosening the knot or cutting the knot.

We talked about Asbury Park. Anti-commandeering cases. Again, I think -- well, the federal government's brief does a much nicer job on this than I ever could in pointing out that the essence of the commandeering cases are the federal direction to state actors -- in this case, maybe it would be state judges or the emergency manager or the governor -- to do something in a particular way. And, in fact, the -- that's not what happens. That is not the structure of Chapter 9 at all. The structure of Chapter 9 is that there is certain power that is vested in this Court, and that power can be used in certain ways. Frankly, your Honor can't tell the city what kind of plan to file, but your Honor can say whether or not you will approve a plan that is filed, so the request has to be made by the city, and the power has

to be exercised by your Honor. Again, the city itself is powerless to escape the contracts clause, but it does not -- at no point does the federal government say I have a policy that I am going to ask the states or demands that the states implement for me. That doesn't happen anywhere in Chapter 9, and, frankly --

THE COURT: Well, but Ms. Ceccotti doesn't agree with that. What she says is Congress says if you want to adjust your debts, we prescribe the priority scheme to the exclusion of the state. The state can't come in with its own notion of what the priorities should be so that the division of sovereignty that results violates the Tenth Amendment.

MR. BENNETT: Well, first, there's a logical failure there, and it has to do with Asbury Park. The UAW starts with the proposition that there is some kind of viable state restructuring process that can actually work and that the federal government took it away from them and made the bankruptcy -- the Chapter 9 exclusive. That isn't reality. Asbury Park, as we've seen, first of all, is an unbelievably exceptional case, which, by the way, the end holding is that that restructuring was done for bonds and made bonds better. That is the holding at the end of the day or the key facts at the end of the day in Asbury Park. Asbury Park is not and never has been construed to be -- and no one cited any case to your Honor showing that in the period of time before

Congress claimed the field for itself that there was any viable municipal debt adjustment opportunity created by what we have to call the Asbury Park exception to the contracts clause. And if you believe everything in the UAW's belief -- brief and believe their interpretation of the pensions clause, it gets even worse, that even if there were -- was Asbury Park wiggle room and then in the absence of the Bankruptcy Code the pensions clause is absolute, you have worse than nothing. You have worse than the almost meaningless Asbury Park exception. So I don't think it's coercion for the -- for Congress to say you can't do something that you can't do. And I think the prohibition on competing state municipal schemes is, frankly, recognition that they're not possible or workable, and, again, no one has been able to show you either before or after that provision of the Bankruptcy Code what this wonderful municipal scheme is out there that would have been a choice. Cardozo doesn't think there's any choice. Bekins doesn't think there's any choice. And that's the same court that decided Ashton, so I -- about the same time actually or Blaisdell was about the same time. Ashton may have been later. This is a -- I think -- I don't think Congress coerced anybody. I don't think that's possible on the facts.

Okay. So to summarize, we've shown that Chapter 9 is constitutional and that, in particular, it does not offend

the contracts clause in the United States Constitution. I think along the way we've demonstrated that the state's authorization of a municipality's resort to Chapter 9 for relief from contracts generally does not constitute a state impairment of contract because otherwise no -- not a single Chapter 9 would work. We have also along the way noted that the filing of a petition itself doesn't constitute impairment of anything in any event and that if there is an impairment, it's by the federal Bankruptcy Court, so now let's look at our contracts clause cheat sheet and try to find out whether there's any difference because of the fact that there's a state contracts clause or because there's a pensions clause.

First, with respect to the state contracts clause, I don't think anyone has suggested to the Court that this is any different than the federal contracts clause, and, in fact, there isn't. There's no difference, and no one suggested it, so -- but, by the way, Justice Cardozo, again, as -- more elegantly and more precisely but -- and the Bekins court both would believe that the state contracts clause -- okay -- is also focused on the state. It doesn't bind the federal government. And since the federal government is the relevant actor, the state contracts clause does not impose any obstacle at all to a municipality invoking Chapter 9 relief.

The only thing I want to pause to say is it couldn't

be otherwise because if it were otherwise -- I skipped a step. Every state -- at least every state I looked at, so there may be an exception, but every state has a state contracts clause. It's not surprising. Copied it from the federal Constitution. So if it were the case that the state's contracts clause was different than the federal contracts clause and that it was a barrier to invoking Chapter 9 relief, then every single bondholder in every single -- I should say every single lawyer for every single bondholder in every prior Chapter 9 case has probably been guilty of malpractice because they might have been able to escape their prior Chapter 9 cases -- and there are now hundreds on the books -- on this basis alone. But, again, for the reasons expressed in Bekins and more elegantly by Judge -- Justice Cardozo, they can't.

So now we finally get -- we reach the pensions clause also quoted in front of you, and we say, okay, is this pensions clause any different than --

THE COURT: But hang on. Isn't there a difference between reconciling the bankruptcy clause with the federal contracts clause on the one hand and trying to reconcile how a state that prohibits itself from impairing contracts with taking advantage of the bankruptcy power that the federal court has enabled -- or that the federal Congress has enabled because of the sovereignty of the state?

MR. BENNETT: No difference. Why? Let's remember. The reason why I spent so much time talking about why was the Debt Adjustment Act under the Bankruptcy Act constitutional as far as the federal contracts clause was concerned -- it wasn't about the language of the federal contracts clause. It was because the state isn't an actor. The federal contracts clause acts only on states. The relevant actor is the federal government. It's the Bankruptcy Court. That was the reason why there was no federal contracts clause problem with the Bankruptcy Act in Bekins, and it was the only reason -- the only part of the opinion that had to do with the federal contracts clause part of the problem. The state contracts clause acts again only on the state, not on the federal government. Accordingly, if you believe -- and the Supreme Court has held that the relevant actor for purposes of untying or cutting the knot is the federal Bankruptcy Court and not the state, then the state contracts clause forms no additional barrier to the use of the Bankruptcy Code than the federal contracts clause did. They are the same, and they are both not relevant for the same reason.

THE COURT: And your position is that it's a matter of federal law that the pertinent actor is the federal court, not the state entity that's in bankruptcy?

MR. BENNETT: The Supreme Court told us along the way to approving the Bankruptcy Act the first -- for

municipalities the first time that it's --

THE COURT: So even if the state law were to say it's the city that's the pertinent actor, that's not relevant because it's a federal law question.

MR. BENNETT: Correct. So for purposes of federal law, the Supreme Court has told us it's the federal Bankruptcy Court that is the relevant actor.

So now we get to the pensions clause, and we've got to find that there's a difference. And I think I want to start here. This is going to be somewhat repetitive of the brief. There's nothing in the pensions clause that says anything like, quote, "and the state shall not authorize any municipality to commence a bankruptcy case that would allow a federal court to impair or diminish pension claims." It just doesn't say that. And, of course, it is words like that that the objectors are saying have to be imported into the pensions clause.

It's hard, I think, because at the end of the day, apart from the fact that the pensions clause is, quote, "more specific," and it's, of course, more specific because they were looking at pensions because the law in Michigan at the time they were looking at the pensions clause was that pensions weren't a contract. That's the only reason it's more specific. It wasn't because -- there's no other evidence for why it was more specific. The only

difference -- the only words that are different are the words, quote, "be diminished." Excuse me. Quote, "diminished or." That's the only difference. "Impaired" is used in all of them. "Prohibition of impairment" is used in all of them. All of them are absolute about prohibitions of impairment.

And I'm going to take this in two steps. First of all, the objectors say --

THE COURT: Well, but hang on. There's the next sentence, which you didn't include on here, the next sentence of the pension clause.

MR. BENNETT: Okay. The funding sentence?

THE COURT: Yes.

MR. BENNETT: Okay. Well, frankly, that's not focusing on today, and it sounds like it's a --

THE COURT: Well, but the objectors argue that this additional consideration that the Michigan Constitution gave to pensions which it didn't give to contracts elevates it, makes it, if not absolute, more absolute than contracts.

MR. BENNETT: Well, let's talk about -- I specifically wanted to talk about that because --

THE COURT: Okay.

MR. BENNETT: -- first of all, why is it -- we should ask ourselves question number one. Why is it that the federal contracts clause and the state contracts clause

became less than absolutely binding? It wasn't because of the inadequacies of the language. It was -- in fact, what the courts have done is they put the word "substantial" in front of the word "contract," so an insubstantial impairment doesn't count, and a substantial impairment has some extra hurdles that you have to go over before you can make it. So, frankly, if what they were trying to do was to tighten the pensions clause and make it more distinctive -- and if they went to the books because, of course, all of the cases, you know, Worthen versus Thomas, Home Building & Loan Association versus Blaisdell, these are like cases from the mid-'30s, so they were all on the books in 1961 through 1963, so they knew that, and they knew that the problem was the incorporation of the substantialness concept. So if they were really after solving that problem, why didn't they just put the words right before "impairment" "substantial or insubstantial impairment"? And they could have tightened it up in the way that it had been loosened. They could have prohibited substantial and insubstantial impairments. That would have dealt with -- if they were trying to say we're opting the pensions out of the judge-made doctrines and exceptions that have burdened the federal contracts clause and the state contracts clause, that's how they might do it.

Now, by the way, it would be irrelevant to this argument because remember the pensions clause, just like the

state contracts clause, just like the federal contracts clause, acts on states and municipalities. It doesn't act on the Bankruptcy Court. It doesn't act on the federal government. And once again, if the right actor -- if the actor that unties the knot or cuts the knot is the federal Bankruptcy Court and the federal government and not the state and not the municipalities, as the Supreme Court says, then the pensions clause, even with the words "substantial or insubstantial" in front of it, doesn't get you all the way home. What they next needed to do in the pensions clause is to say by enacting the pensions clause and giving it -- and making pensions special, we now want to do something else. We really want to say -- objectors thinks the Constitution -- that the convention -- that the conventioneers really wanted to say, well, in a municipality that has material pension claims, they can't resort to a federal court to seek relief. That's what they really want us to find in the pensions clause. But, frankly --

THE COURT: No, no. I don't hear that at all. What I hear is you are welcome to come in that door so long as the city's assets, according to Mr. Dusen, are first allocated to pensions.

MR. BENNETT: Well, if there was a lawyer around there at the constitutional convention who was doing research -- and I suspect that there was -- they should be

charged with figuring out that the only way to stop the federal courts -- if there is even a way, but the only way to stop federal courts from having the power to impair contracts that maybe a state can't impair is to cut off the -- is to basically say the state cannot ever go to a federal court for a federal -- then it was called composition, you know, federal debt composition case.

And the other point that your Honor should note is that -- and we say this in our papers -- during the entire constitutional convention, for years before and almost continuously thereafter, the State of Michigan had authorized the municipalities to file Chapter 9 cases, so if they were really elevating pensions in the way of taking them -- distancing themselves from the federal power to impair them and they knew, open paren, one, that the federal debt composition scheme had been determined to be constitutional by the Supreme Court in part because the federal court was doing the work of impairing contracts and they knew -- they have to be presumed to know that Michigan had opted in and had continuously all through the period -- in fact, I think in our papers we say when they repealed it. I think they repealed it around 1980 when general authorization was all that was necessary, so they kind of covered the entire period. No one ever said, gee, we better as hell change this. And in all of the legislative history of the

constitutional convention, you don't have a word about bankruptcy and pensions, and the words that you do have -- the words that were quoted to you in the papers just filed -- I have to find it. Okay. Here's AFSCME's best quote from the official record of the constitutional convention, 2 Official Record, page 3402. This is a new section that requires that accrued financial benefits of each pension plan and retirement system of the state and its political subdivisions be a contractual obligation which cannot be diminished or impaired by the action of its officials or governing body. It's in AFSCME's papers, paragraph -- the new ones, the supplemental papers. Actually, those are amended and restated, paragraph 19, page 11. Same brief, paragraph 142, page 71. Pension benefits constitute, quote, "deferred compensation for work performed which should not be diminished by the employing unit after the service has been performed," close quote. Those are the quotes that you were offered by AFSCME about the seriousness and importance of the work done in the constitutional convention from 1961 to 1963, this against the background where it's been the law of the land, at least as far as the Supreme Court is concerned, since 1930 -- I can't remember exactly.

THE COURT: So is it your view that the only effective way that the Michigan Constitution could have provided the protection for pensions that the objectors seek

here is by the Constitution prohibiting a Chapter 9 filing?

MR. BENNETT: Prohibiting authorization of a Chapter 9 filing or -- yes, your Honor. That's exactly what they would have had to do, and that's not the kind of thing that they can do by implication.

I want to talk a little bit more because I think there's a lot of stress that's put on the words "diminished or," and there is the assertion that "diminished or" has to be given some meaning, but, frankly, the only meaning it could be given is to somehow expand "impaired." I don't personally think it does expand "impaired," and there's -- I want to point out before moving on with a whole bunch of authority to that effect that it's really dangerous for a court to decide that "diminished or" added anything to "impaired" because if the Court decides that "diminished or" filled some gap that's related to the word "diminished and impaired," then in the next case someone is going to come to your Honor and say, "You know that state contracts clause? There's no 'diminished' there, and 'impaired' has to mean less than 'diminished or impaired' in the pensions clause." So it's actually a good thing that there's law out there on this subject -- we had it in our brief -- that basically says that if you run into one of these problems where you've got a list and you want to say that they all have an independent and separate meaning, you've got to propose an independent

and separate meaning for the terms on the list that actually solve the problem. And in this case, trying to find an extra meaning for "diminished or" -- again, it's consistent with its place in the sentence -- does -- creates a mess in the state contracts clause in Article I, Section 10.

Apart from that, it turns out that when you go look at the books -- and this is not in our papers because this was an issue raised in the responsive papers -- is that every time we found the definition of "impair" in the cases or in dictionaries, it includes diminishment, which should not be terribly surprising. It's a very common sense answer. But if you want a list -- and you might need them in connection with putting together an opinion -- you could start with the Bank of Minden case, which is a Supreme Court case, 256 U.S. 126 at 128. Then if you want to go to the Sixth Circuit, Riverview Health Institute, 601 Fed. 3d 505. Black's Law Dictionary, Webster's Third, and then there's a bunch of state courses -- state cases from other states that all say the same thing. I could read the quotes, but I'll save the time because it really is kind of a commonsensical -- a common -- it's common sense that "impaired" has to include "diminished." "Impaired" is much broader than "diminished," and every so often this is either a -- there's a rhetorical flourish that works its way in, and this may well be what that is, and that's all it can be.

Okay. Moving on to the issue of whether or not the authorization to file Chapter 9 is ineffective because the emergency manager or the governor recognized that impairment of pension benefits may be necessary. I don't want to add additional arguments to the constitutional provisions. That's not the purpose of this section. The purpose of this section is to deal with the point made, I think, by only one or two of the objectors that the -- that there's an instruction to the emergency manager to comply with the pension statute, and that should apply to the filing of a Chapter 9 case as well. I'm sure your Honor has your own copy of the Local Financial Stability and Choice Act, Act 436, and when you look at the -- most importantly, when you look at the Chapter 9 authorization section, there is no instruction that the emergency manager comply with the protections affecting pensions. By the way, that may well make sense. There are a whole bunch of other provisions that talk about what the emergency manager is supposed to do out of court, and not surprisingly it talks about him having to comply with many laws and to pay many debts and to do many things. He resorts to Chapter 9 when he can't accomplish those things out of court. And if one thought that anything about the emergency manager law meant to say that the emergency manager had to in Chapter 9 continue to not impair pensions, you would think it would belong in the section that

is applicable when the emergency manager files Chapter 9.

In addition, I think the part that was read to your Honor earlier this morning has a lead-in clause that didn't make it into the record. It reads, "If the emergency manager serves as sole trustee of the local pension board, all of the following should apply," and that's where the provision that was located was read to you, so there is nothing in the emergency manager law -- and, in fact, the structure of the emergency manager law itself suggests that a lot of bets are off in a Chapter 9 context that may not be -- including things that the emergency manager is supposed to try to accomplish if he's in an out-of-court world.

Next argument, failing to condition authorization on nonimpairment of --

THE COURT: One second. Does that suggest that in order to accomplish what Mr. Orr thinks is necessary to accomplish with regard to pensions, he needs to be a trustee of the plan?

MR. BENNETT: No. It's that -- no. He has the right to remove trustees of the plan for other purposes, and these are these extra requirements that are imposed upon him just in those circumstances that it -- I think when your Honor gets a chance to look at it -- what did I do with it? I had it here a second ago, so I'll give you -- let me give the exact section referenced so it's easy to find.

THE COURT: Okay.

MR. BENNETT: The part I read from is in Section 12(m), and it is confined to that relatively narrow circumstance.

Okay. First of all, on the issue of whether or not the governor's failure to put conditions on authorization makes the authorization invalid, we indicate in our brief that we don't think that conditions on authorization could be valid, that -- and as I think -- I think I got ahead of myself earlier, so I don't want to take too much time in covering it again now, but we're talking here about one of the core subjects of bankruptcy, which is priorities, who gets paid when there's not enough to go around. If that's not a core subject of bankruptcy -- not in the core versus related, but if that's not the absolute center of the subject of bankruptcies, I don't know what it is. And we've cited a lot of law, and your Honor has pointed out there are many cases, none decided the other way, that say particularly in the context of things touching on priorities and who gets paid first and who gets paid second, who doesn't get paid at all, that the -- that you buy the Bankruptcy Code as a whole. You buy the scheme as a whole. You don't buy parts of it. And in this sense federal law is supreme because once there is a proper bankruptcy case before the Court, it is the federal priority scheme that applies. It is legitimate that

the federal priority scheme applies because it's legislation on the subject of bankruptcies, and because it's legislation on the subject of bankruptcies, it is absolutely supreme, period, end of story.

So, as to your Honor's hypothetical, if anyone walks into the federal court and says, "I want federal judicial relief. I want to use that federal power to untie and cut knots, but I want the ultimate distribution or really any part of the distribution to be conducted in accordance with my terms," whether they're found in a statute or in a state Constitution, it doesn't matter. The federal law on this issue is supreme, and it's supreme over Constitutions and over statutes, period, end of story.

It seems kind of small when done with that to point out that 436 permits but doesn't require conditioning. We can imagine a whole bunch of conditions that might have been very sensible and that might not offend federal jurisdiction like it could have been -- there could have been suggestions or requirements as to exactly how the emergency manager should interact with other elected representatives or with other people. Actually, the governor does have one -- it's not quite a condition. It's a suggestion, but I think he'd be offended if it wasn't followed, which is he wants Mr. Orr to continue to communicate with the governor and the treasurer relating to what he's doing. So I think we can

think of several things that could be -- that you could use for the PA 436 conditioning power that would be perfectly okay, but going in and saying, "Gee, as a matter of this particular state law" -- and, by the way, it's -- the governor would -- to do that, he's got to ignore the conflicts that I discussed earlier between a law that says thou shall not impair this one with another law that says you're the first money out. It's mind-boggling what he'd have to reconcile, but the instruction would be, yeah, this one we really meant and the others we didn't really mean, follow that one first. I think that that would be an invalid authorization. I think the Court would have to say that authorization isn't okay for federal court purposes. I think as a prudential matter, the federal court should not get involved in a case where the authorization is conditioned in a way that would offend the federal scheme, but understanding that there may be very extreme and difficult circumstances involved, a creative federal court might want to give people some time to kind of take a couple steps back and figure out how to do it better.

THE COURT: Let me ask about Section 943.

MR. BENNETT: I need to get a case if you're going to do that because I -- from the --

THE COURT: This is the Bankruptcy Code.

MR. BENNETT: Yeah.

THE COURT: 943(b)(4).

MR. BENNETT: Right. There's actually one case that's dealt with that previously, and I think it's --

THE COURT: Let me just get my question out.

MR. BENNETT: Okay.

THE COURT: Thank you. So the question is what does this section mean if it doesn't mean that the state can dictate the priorities?

MR. BENNETT: Because it says "from taking any action necessary to carry out the plan," and I --

THE COURT: What does that -- what does that language mean? What meaning does it have? How does it come into effect?

MR. BENNETT: Okay. I think the best way to work through that is the Sanitary Improvement District Number 7 case, 98 B.R. 970, and this is a really fascinating case because the facts gave you every conceivable issue under the sun in terms of the interpretation of this section. What happened in Sanitary Improvement District is that the debtor had -- you know, had claims against it. Let's call them a hundred. I'm using representative numbers, not the actual numbers. As a result of the bankruptcy case, they issued paper, and I think it was like 60. Okay. And the -- but the paper that was 60 had in it a provision that said that if the debtor paid it in full within a certain number -- within a

certain number of months -- I think it was 18 months -- after the bankruptcy case is over, it only had to pay 95 cents on the dollar or something like that, and so the creditors came in, and they attacked the whole plan, pointed to a state law that says thou shall pay your bonds. By the way, there are laws like that in Michigan, too. And the court decides very easily that the takedown from a hundred to 60, well, that's supremacy clause bankruptcy. You can do that notwithstanding state law. What you can't do, though, is because state law says you have to pay bonds at a hundred percent of principal, you can't have the five-percent discount feature because that's -- after the bankruptcy, you issued this new bond, you know, with 60 being the new hundred, but you've said that you can still pay that off at a discount. That violates 943(b)(4). So what this case illustrates is that this looks at the obligations after they've been restructured and says that the Bankruptcy Court does the restructuring. By the way, very consistent with the Cardozo and the Bekins view of the world, you -- and you're finished. The bankruptcy -- there's a confirmation order. New instruments are issued. Those instruments, the ones that you walk out of Bankruptcy Court with, have to be instruments that you can perform in accordance with state law.

THE COURT: So this provision, in your view, says nothing about the requirement of the plan itself or the order

confirming plan to comply with state law.

MR. BENNETT: I don't know if there's any case that says that. There may be. I think Sanitary and Improvement District Number 7 has got it right, that it does not say anything about the Bankruptcy Code restructuring process. It only acts on the debt that is issued after the case is over.

I don't think I have to spend time on it, so I'm going to skip over -- again, it's in our papers. There's an assertion in the papers that the Tenth Amendment is not reserved -- that the Tenth Amendment reserves every issue relating to municipal pensions to the states. I think we've dealt with that enough in the constitutional section, and I don't have to deal with -- this really is the -- an argument was built, constructed based upon the fact that in the case of ERISA the federal government didn't make ERISA -- didn't make states or municipalities applicable to ERISA, didn't create the insurance program, PBGC, and the assertion is made because the federal government chose not to go into those areas, they must have done that because they were absolutely precluded from doing so, ergo they are precluded from using the bankruptcy power to modify pensions. I think that fails logically in a lot of places, but most importantly maybe to start with is that it's not clear that there is no possible way for the federal government to apply the ERISA statute or the PBG statute to state municipalities, maybe to states but

not to municipalities, and -- at all, by the way, and that Congress didn't may have reflected political realities at the time and not actual constitutional limitations, so I think the starting point of that argument just fails, and I think we've seen that federal -- that a federal bankruptcy power can be applied by the federal court to obligations. Pensions are clearly within the federal bankruptcy power, no dispute in the private context. There's nothing different about Chapter 9 context. And so there is no such part of the Tenth Amendment that constrains this aspect of the subject of bankruptcies.

The next point is a really important one, and I could easily have started with it, and I know your Honor has been concerned with it throughout, which is whether or not your Honor really has to deal with the -- whether or not pensions can be impaired in bankruptcy in the context of authorization. I hope it's clear to your Honor that the city is perfectly comfortable with you dealing with it now or perfectly comfortable with dealing with it later. We don't think that this is -- some of these things may be a little bit conceptually difficult and complex, but the constitutional law on the subject is really pretty clear, and so we're prepared to have it decided. We think that there's only one way to decide it. There is, though, a way for your Honor to decide not to decide it, which is to find -- and the

next to the last sentence I read from Justice Cardozo in his dissent where he says, "just the filing is not doing anything," we say that, too. It is starting a bankruptcy case. I have said at the beginning -- I mean it -- there is nothing inevitable. A cramdown of revisions to pension benefits, a cramdown of a particular treatment of the underfunded portion of the pension obligation is not necessarily the way this case is going to end, and it's not necessarily the next step in this case. We just don't know. The next -- obviously right now mediation is an important milestone. The next important milestone is the plan, and since your Honor has been around the Bankruptcy Courts for a good long time, you know that the plan that we file before the end of this year is not likely to be the plan that we ultimately confirm. It would be actually a good exercise for different people to figure which amended plan is going to be the plan. The bottom line is nobody really knows. And so it is possible to adopt Justice Cardozo's view that no change in obligation results from the filing of a petition by one seeking a discharge whether a public or private corporation invokes the jurisdiction and basically say since nobody has done anything yet, we're not going to decide anything more. You could do that. I will say that the -- I think that the assertion that there is an imminence that -- an imminence of harm represented by the filing of the Chapter 9 case that

requires this Court to act is, frankly, not a fair statement of the law. I think one of the more important cases is Donohue. It's been cited by objectors. The most important part -- Donohue is the Nassau County financial restructuring case, and the most important part of Donohue that led the Court to act I think is mentioned by the Court. It's kind of near the end of the opinion. The Court says the law, the ordinance that gave the county executive all the powers, "provides expansive and seemingly limitless power to the County Executive without any reasonable restraints other than the procedural mechanism of an executive order." This case would be a lot simpler if all Kevyn Orr had to do to reorganize the debts of Detroit was to say how he wanted to do it and sign it as an order. He doesn't think he has that power. I don't think he has that power. No one in this room thinks he has this power. We've talked about the fact that to get to a debt adjustment plan that is nonconsensually confirmed, it has to be filed. There has to be disclosure statement approved. There has to be voting. There has to be more discovery. There has to be a confirmation hearing, and there has to be an order of this Court. That is a very different procedure or array of protections than was available in the Donohue case, which is, frankly, the closest case to this one in terms of the kinds of things that we're talking about here. If your Honor goes through the other

cases that have been cited for the proposition of imminent harm, you will find that in all of them there was no judicial step going to occur before the harm might be inflicted. In all of --

THE COURT: Let me ask that question here. Can you -- are you willing to identify here on the record or can you identify here on the record any conceivable circumstance in which retiree benefits, pensions won't be impaired by a plan?

MR. BENNETT: You know, your Honor, at this point there are a number of major things that I don't know, and I will say I don't know that there won't be money from outside, although I tend to doubt it. I don't know that. I do not know whether there will be -- whether certain other assets will, in fact, be available to the city to address its debts, and I will point out in this regard that while the objectors have cited over and over and over again a pleading filed by the attorney general asserting the primacy of pension claims, they've all managed to have forgotten a formal opinion he's given concerning the accessibility of certain assets in this bankruptcy case, particularly the art, and -- but I have no idea, number one, what's going to happen with that, and I have no idea what the -- whether or not there will, in fact, be a transaction involving the departments of water and sewerage and whether those transactions will deliver material

dollars. So while I'd be kidding myself and kidding the Court and kidding everyone here if I said that I thought it was anything but likely that there would be some impairment of the underfunding claims in this case, it's not fair to ask me and I don't think I could say that there's no scenario where impairment will not be necessary. I just don't think I can even say that today.

THE COURT: Okay. Even with that much of a disclosure here, why isn't that enough to say there's an impairment here?

MR. BENNETT: I'm sorry.

THE COURT: Why isn't that enough to say at this point in time there's an impairment?

MR. BENNETT: Well --

THE COURT: There's a sufficient impairment to get past ripeness anyway.

MR. BENNETT: You know, I don't think you can say there's impairment because the Supreme Court has told us there is not. There won't be impairment, your Honor, until you say so. Is there a risk of impairment? There's a risk of impairment. Is the risk of impairment enough to make this ripe? And the answer is is that -- I think this is the answer when -- I mean the Donohue case is a good example, but I think it ripples through all the others, which is that if a court is presented with a situation where there's a risk of

impairment and the impairment can occur before there's another opportunity or requirement that people show up in front of a judge, then they start thinking about whether there's interim harm, but there's not a single case that has been cited to you that says there is imminent harm in circumstances where no one is going to suffer anything until and unless a court enters an order after notice, opportunities for discovery, opportunities for hearing, and all the other protections that are available in connection with a plan confirmation process in a Bankruptcy Court. It's just totally different. The cases are dealing with a totally different situation, particularly the Donohue case.

Do you have -- we're 20 minutes to.

THE COURT: Twenty till five.

MR. BENNETT: Do you want to save time for your questions or --

THE COURT: If you want to stop now, and we'll pick it up with the government's attorney, that's fine with me, and then we'll pick up the balance of your argument tomorrow. Is that what you're --

MR. BENNETT: I think it's a good break point.

THE COURT: Okay.

MR. BENNETT: I have very minor things left.

THE COURT: Good.

MR. TROY: Matthew Troy, your Honor, Department of

Justice, Civil Division, on behalf of the United States. If it makes any difference to your Honor or the other parties, I am here for tonight and can be available tomorrow as well.

THE COURT: I appreciate that, but since you're here, let's have at it.

MR. TROY: Fair enough.

THE COURT: Well, my primary questions relate to how you address the arguments here that the objecting parties made in response to your brief regarding ripeness.

MR. TROY: To be honest with you, your Honor, I've only reviewed those very quickly because I filed the brief on Friday and then went back to furlough status. And on Monday --

THE COURT: That.

MR. TROY: And on Monday --

THE COURT: Well, would it be your preference to have overnight to think about how to respond to the objectors' concerns regarding ripeness?

MR. TROY: Sure. I can do that.

THE COURT: Would that be your preference?

MR. TROY: That would be, yeah, a more fulsome discussion, I think.

THE COURT: All right. Then you are excused, and I will hear from you tomorrow regarding that. Do you want to stop for the day now and pick it up tomorrow?

MR. BENNETT: Your pleasure, your Honor. I can keep going, but I can also stop. I'm not going to -- I don't have -- less than 30 minutes left, in fact, significantly less than 30 minutes left.

THE COURT: Well, do you think you can finish in the 20 minutes that are left before five?

MR. BENNETT: I'll try.

THE COURT: All right. Then I would invite you to try.

MR. BENNETT: Let me just get a little bit reorganized. Okay. The next topic on my list is collateral estoppel, and, your Honor, I think with respect to collateral estoppel, a couple of points are worth focusing on. First of all, our very, very first point on this -- and I think it's dispositive -- is that when this case was filed, this Court had the most exclusive jurisdiction it ever gets about anything, absolutely exclusive interest -- exclusive jurisdiction under 1334(a) to decide matters in the case, and eligibility is a matter in the case. And the assertion by the objectors is that the Webster court really didn't decide eligibility. The Webster court was deciding some abstract issues of state law. And, your Honor, two things. Number one, the objectors can't even say that without mentioning the eligibility determination, and here I'm looking at the funds -- Mr. Gordon's brief at page 32. The Webster judgment

rules squarely on the constitutionality of PA 436 and the governor's authorization of the emergency manager to proceed under Chapter 9 in light of the pensions clause of the Michigan Constitution. There was absolutely no confusion in the judge's mind or anyone around that courtroom's mind that what they were trying to do was to get an early determination of eligibility. It might have succeeded, but this case was actually filed first. And by the way, although the attorney general will probably have more to say about this, there was no adjournment sought for purposes of filing the Chapter 9 case, and the transcript shows no such thing. And they know more about the circumstances than I do, and they can address it tomorrow when it's their turn.

But there's an even more important point, which is that the order that was entered by the judge purports to enjoin the emergency manager directing him to have the case dismissed and not file another one, so I just -- I can't abide the assertion and the record does not support the assertion that what happened in that court was not an effort at an eligibility determination, so, number one, that was within the exclusive jurisdiction of this Court. If it was within the exclusive jurisdiction of this Court, it wasn't within the jurisdiction of that Court to do anything about it, and, therefore, any judgment that was entered after the filing for that reason alone is void.

Now, second point we make is that the automatic stay applied as well because the entire event, even though the city was not a party, was an effort to gain control over the city's assets and an effort to enhance collection of the debt. Again, there can't be much dispute about that, open paren, one, partly because of the way the whole proceeding evolved and how everyone understood it, but more importantly, here again we have the judge explicitly talking about the Chapter 9 case and attempting to stop the Chapter 9 case because of the perception that the Chapter 9 case might impair pensions, and those kinds of acts are clearly within the automatic stay. Again, I think that the --

THE COURT: Just to be clear, you're talking about the automatic stay of Section 362 --

MR. BENNETT: Yes.

THE COURT: -- the Bankruptcy Code.

MR. BENNETT: Correct, the Bankruptcy Code's automatic stay, or 942. The other half of it is in the -- is in Chapter 9 as well.

Full and fair opportunity to litigate. Again, I would ask the Court to look at the record in that case. There had been -- it is certainly true that a whole bunch of briefs that were filed -- I don't think the hearing where this all occurred had previously been calendared and noticed to anybody. The hearing was set on an emergency basis, and

someone got on the phone and called for the attorney general's office because they thought it might be a good idea to tell him about it about an hour before the hearing. That's actually not the way things are fully and fairly litigated in any courts I visit, and I don't think that when your Honor ticks through the procedural elements of what happened in that case in Lansing is going to be convinced that there was a full and fair opportunity to litigate.

THE COURT: Let me ask you just a sort of administrative question regarding this. Do we have in our record here all of the pleadings and papers and dockets and transcripts from that case?

MR. BENNETT: I don't know if they're there yet.

MS. NELSON: I believe I can answer that, your Honor. Assistant Attorney General Margaret Nelson. It's my understanding, no, those have not been submitted. I do have all of the transcripts, which I was prepared to present to the Court when I make my argument, which now appears to be tomorrow. If the Court would like the submission of the pleadings, we'll be happy to do that, although it's --

THE COURT: Well, my understanding is that some of the pleadings have been attached to various briefs, but I'm just not sure if it's everything.

MS. NELSON: There was only a -- there was --

THE COURT: Just to --

MR. BENNETT: We'll get it in.

THE COURT: Yeah, exactly. Just to be complete --

MS. NELSON: Yes.

THE COURT: -- let me make my request to you that our record here include everything from that case, including the docket.

MS. NELSON: There's three cases, your Honor.

THE COURT: Okay.

MS. NELSON: And so -- that were filed separately --

THE COURT: Well, but I think the --

MS. NELSON: -- so I will submit everything --

THE COURT: I think the one that's at issue here is the one in which a judgment was entered.

MS. NELSON: Correct.

THE COURT: That's the one I need.

MS. NELSON: So you want everything in the case in which the judgment was entered the next day, including the docket entries.

THE COURT: Thank you.

MS. NELSON: Would you also like the Court of Appeals materials --

THE COURT: Yes.

MS. NELSON: -- because the Court of Appeals materials were --

THE COURT: Yes.

MS. NELSON: -- filed and a stay order entered thereto?

THE COURT: Just for --

MS. NELSON: Webster?

THE COURT: For completeness, yeah. All right. I have to -- I have to pause here. I've been advised that the people in our overflow room couldn't hear this exchange, so I will just restate it for the record. The attorney general's representative has agreed to provide to the Court in this case the complete record from the Webster litigation not only at the trial court level but at the Court of Appeals level, including all pleadings and papers, transcripts, and docket entries, the docket itself. You may proceed, sir.

MR. BENNETT: Okay. Lastly, the last factor with respect to collateral estoppel, your Honor, is the issue of whether or not the judgment would be binding on the city in any event. Of course, the city was not a party to those proceedings. The assertion is made that the -- that there is privity between the city and the state because they have a common legal interest in some matters in connection with this Chapter 9 case. Frankly, I don't think those are the same standard, and I think we covered that in our papers, but I will say one other thing is that to the extent that there -- that the plaintiffs in those cases believed that the city was in privity with the state with respect to those cases is an

additional reason why the automatic stay applied from the very beginning because if they thought that they were in a case with the state really trying to bind the city, then it is perfectly clear that they violated the automatic stay.

I don't think I have any other material topics that I think we need to cover based upon the argument by others. If I've missed something or if your Honor has any questions, I'd be happy to take them. Otherwise I'll allow the attorney general to take the floor tomorrow.

THE COURT: Um-hmm.

MR. BENNETT: We'll be done early.

THE COURT: Okay. Good. We'll be in recess now until 10 a.m. tomorrow morning.

MS. NELSON: Your Honor, before you leave the bench, may I just ask do you want those pleading -- do you want everything submitted electronically?

THE COURT: Yes, yes, in the record of this case. Thank you.

THE CLERK: All rise. Court is adjourned.

(Proceedings concluded at 4:51 p.m.)

INDEX

WITNESSES:

None

EXHIBITS:

None

I certify that the foregoing is a correct transcript from the sound recording of the proceedings in the above-entitled matter.

/s/ Lois Garrett October 20, 2013

Lois Garrett